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FEDERAL TRADE COMMISSION DECISIONS

FINDINGS, OPINIONS, AND ORDERS

JULY 1, 1980 TO DECEMBER 31, 1980

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MEMBERS OF THE FEDERAL TRADE COMMISSION AS OF DECEMBER 31,1980

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Took oath of office April 21, 1977

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Took oath of office March 21, 1961

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Took oath of office August 26, 1976

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Took oath of office June 29, 1978

PATRICIA P. BAILEY, *Commissioner*
Took oath of office October 29, 1979

CAROL M. THOMAS, *Secretary*
Appointed June 20, 1977

CONTENTS

	Page
Members of the Commission	II
Table of Cases reported	V
Findings, Opinions, and Orders	1
Table of Commodities	1127
Index	1129

TABLE OF CASES

The names in SOLID CAPITALS refer to cases in which orders to cease and desist have been entered by the Commission, and also to interlocutory orders and modifying orders, which are indicated in parentheses. The names in *italics* are cases which the Commission has dismissed.

Dkt. No.	Name	Page
9046	AKTIEBOLAGET SKF (Modifying order)	752
8904	*Allied Grape Growers*	385
C-3050	AMERICAN ART CLAY CO., INC.	809
9126	APPLEBAUMS FOOD MARKETS, INC.	42
9089	ATLANTIC RICHFIELD COMPANY (Modifying order)	600
8827	BATTEN, BARTON, DURSTINE & OSBORN, INC. (Modifying order)	380
C-3042	BENDIX CORPORATION, THE	352
C-3032	BENEFICIAL CORPORATION, et al.	120
C-3032	BENEFICIAL MANAGEMENT CORPORATION	120
C-3044	BENTON & BOWLES, INCORPORATED	619
C-3030	BILL CROUCH FOREIGN, INC. (d/b/a Bill Crouch Imports, Inc.) (formerly Mazda of Boulder, Inc.)	111
C-3045	BINNEY & SMITH INC.	625
C-3037	BLAIR, CLAUDE M.	184
C-3026	BOB RICE FORD, INC., et al.	18
8908	BRITANNICA HOME LIBRARY SERVICES, INC. (Modifying order)	778
9028	BRUNSWICK CORPORATION, et al.	151
C-3033	CHRYSLER CORPORATION	134
9074	CHUCK OLSON CHEVROLET, INC.	37
C-2586	C. ITOH & CO. (AMERICA), INC. (Modifying order)	40
C-3027	CLINIQUE LABORATORIES, INC.	51
C-2717	COMMERCIAL COLLECTORS (Modifying order)	825
C-2717	COMMERCIAL SERVICES COMPANY, INC., et al. (Modifying order)	825
8919	DANCER-FITZGERALD-SAMPLE, INC.	1
8919	DANCER-FITZGERALD-SAMPLE, INC. (Interlocutory order)	205
C-3034	DARVEL, INC.	145
9108	E. I. DUPONT DE NEMOURS & COMPANY (Interlocutory order)	650
9108	*E. I. DuPont de Nemours & Company*	653

		Page
8908	ENCYCLOPAEDIA BRITANNICA, INC., et al. (Modifying order)	778
8954	EQUIFAX INC.	844
C-3052	FARNUM COMPANIES, INC., et al.	826
9046	FEDERAL-MOGUL CORPORATION (Modifying order)	752
C-2600	FIDELITY FINANCE CO., INC. (West Coast Credit Corporation d/b/a) (Modifying order)	823
9105	FORD MOTOR COMPANY	362
9073	FORD MOTOR COMPANY, et al.(Modifying order)	32
9073	FORD MOTOR CREDIT COMPANY (Modifying order)	32
9073	FRANCIS FORD, INC. (Modifying order)	32
C-3028	FRED MEYER, INC.	60
8883	GENERAL FOODS CORPORATION (Interlocutory orders)	91, 605
9085	GENERAL FOODS CORPORATION (Interlocutory orders)	162, 168
8883	GENERAL MILLS, INC. (Interlocutory orders)	91, 605
9074	GENERAL MOTORS ACCEPTANCE CORPORATION	37
9074	GENERAL MOTORS CORPORATION, et al.	37
C-3049	GENSTAR LIMITED	795
9016	GIBSON, HERBERT R., SR., et al. (Modifying order)	126
8879	GROLIER, INCORPORATED, et al. (Interlocutory order)	332
8904	*Hueblein Allied Vintners, Inc.*	385
8904	*Hueblein, Inc., et al.*	385
8883	KELLOGG COMPANY, et al. (Interlocutory orders)	91, 605
9110	LASALLE EXTENSION UNIVERSITY	208
C-3031	LESKO, TERRANCE D., M.D.	73
8919	LOIS HOLLAND CALLAWAY, INC. (Interlocutory order)	205
9110	MACMILLAN, INC., et al.	208
9028	MARINER CORP.	151
C-3047	MENTHOLATUM COMPANY, INC., THE	757
C-3035	MIDLAND-ROSS CORPORATION	172
C-3046	MILTON BRADLEY COMPANY	638
C-3053	MURATA MANUFACTURING CO., LTD.	1116
C-3038	MUSHAM, WILLIAM C.	189
C-3036	NARCO SCIENTIFIC, INC.	178
9126	NATIONAL TEA COMPANY, et al.	42

		Page
C-3039	PAY LESS DRUG STORES NORTHWEST, INC.	197
C-2986	SCHERING-PLOUGH CORPORATION (Modifying order)	194
9046	SKF INDUSTRIES, INC., et al. (Modifying order)	752
C-3043	SMITHKLINE CORPOATION	612
8827	STANDARD OIL COMPANY OF CALIFORNIA, et al. (Modifying order)	380
8919	STERLING DRUG INC., et al. (Interlocutory order)	205
9097	TENNECO, INC. (Interlocutory order)	346
C-3041	TINGLEY RUBBER CORP.	340
C-3040	totes incorporated	335
C-3029	TOWLE MANUFACTURING COMPANY	83
9059	TRANS WORLD ACCOUNTS, INC., et al. (Modifying order)	196
8904	*United Vintners, Inc.*	385
C-3048	UNIVERSAL BODYBUILDING, INC., et al.	783
C-2600	WEST COAST CREDIT CORPORATION (d/b/a Fidelity Finance Co., Inc.) (Modifying order)	823
9028	YAMAHA MOTOR CO., LTD.	151
C-2908	ZAYRE CORP. (Modifying order)	603

FEDERAL TRADE COMMISSION DECISIONS

Findings, Opinions and Orders

IN THE MATTER OF

DANCER-FITZGERALD-SAMPLE, INC.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF SECS. 5 AND 12 OF THE FEDERAL TRADE COMMISSION ACT

Docket 8919. Complaint, Feb. 23, 1973—Decision, July 1, 1980

This consent order requires, among other things, a New York City advertising agency to cease disseminating advertisements which misrepresent, or fail to make relevant disclosures regarding the contents, performance, effectiveness, or therapeutic superiority of Bayer Aspirin, Bayer Children's Aspirin, Cope, or similar non-prescription drug products manufactured by Sterling Drug Inc. Additionally, the order requires the firm to substantiate all representations made for non-prescription drug products concerning their performance, effectiveness and freedom from side effects.

Appearances

For the Commission: *Melvin H. Orlans, H.R. Field, C.B. Anaeer, R.B. Bloomfield, D.J. Freeman* and *Joel Brewer.*

For the respondent: *Richard Rieder, Dunnington, Bartholow & Miller,* New York City.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that Sterling Drug Inc., a corporation, Dancer-Fitzgerald-Sample, Inc., a corporation, and Lois Holland Callaway, Inc., a corporation, hereinafter referred to as respondents, have violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. For purposes of this complaint the following definitions shall apply:

1. "Commerce" means commerce as defined in the Federal Trade Commission Act.

2. "False advertisement" means false advertisement as defined in the Federal Trade Commission Act.

PAR. 2. Respondent Sterling Drug Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware with its office and principal place of business located at 90 Park Ave. in the City of New York, State of New York.

Respondent Dancer-Fitzgerald-Sample, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware with its office and principal place of business located at 347 Madison Ave. in the City of New York, State of New York.

Respondent Lois Holland Callaway, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York with its office and principal place of business located at 745 Fifth Ave. in the City of New York, State of New York.

PAR. 3. Respondent Sterling Drug Inc. is now and has been for all times relevant to this complaint engaged in the manufacturing, advertising, offering for sale, sale and distribution of certain nonprescription internal analgesic preparations which come within the classification of drugs as the term "drug" is defined in the Federal Trade Commission Act. The designations, directions for use and active ingredients for some of these analgesic drugs are as follows:

1. *Designation:* "Bayer Aspirin"
   Active ingredients:
   Aspirin
   Dosage: 1 or 2 tablets with water every 4 hours, as necessary, up to 12 tablets a day.
2. *Designation:* "Bayer Children's Aspirin"
   Active Ingredients:
   Aspirin
   Dosage: Varies depending upon age of child.
3. *Designation:* "Cope"
   Active Ingredients:
   Aspirin
   Caffeine
   Methapyrilene Fumarate
   Magnesium Hydroxide
   Aluminum Hydroxide (Dried Gel)
   Dosage: 1 or 2 tablets every 4 hours, as needed, up to 9 tablets per day.

4. *Designation:* "Vanquish"
Active Ingredients:
Aspirin
Caffeine
Acetaminophen
Magnesium Hydroxide
Aluminum Hydroxide (Dried Gel)
Dosage: 2 caplets with water. Can be repeated every 4 hours if needed, up to 12 caplets per day.
5. *Designation:* "Midol"
Active Ingredients:
Aspirin
Caffeine
Cinnamedrine HCL
Dosage: 2 Midol Tablets with water. Repeat 1 or 2 tablets every 4 hours as needed, up to 8 tablets per day.

PAR. 4. Respondent Dancer-Fitzgerald-Sample, Inc. is now and for all times relevant to this complaint has been an advertising agency of Sterling Drug Inc., and for all times relevant to this complaint, has prepared and placed for publication, advertising material, including but not limited to the advertising referred to herein, to promote the sale of the said "Bayer Aspirin," "Bayer Children's Aspirin" and "Cope."

Respondent Lois Holland Callaway, Inc., for all time relevant to this complaint has been an advertising agency of Sterling Drug Inc., and for all times relevant to this complaint, has prepared and placed for publication advertising material, including but not limited to the advertising referred to herein, to promote the sale of the said "Vanquish."

PAR. 5. In the course and conduct of its aforesaid business, respondent Sterling Drug Inc., causes the said analgesic drug preparations, when sold, to be transported from its places of business located in various States of the United States to purchasers thereof located in various other States of the United States and in the District of Columbia. Respondent Sterling Drug Inc., maintains and at all times relevant to this complaint has maintained, a substantial course of trade in said preparations in commerce. The volume of business in such commerce has been and is substantial.

PAR. 6. In the course and conduct of their businesses, respondents Sterling Drug Inc., Dancer-Fitzgerald-Sample, Inc., and Lois Holland Callaway, Inc., have disseminated, and caused the dissemination of, certain advertisements concerning the said drugs by the United

States mails and by various means in commerce, including but not limited to, advertisements inserted in magazines and newspapers, and by means of television and radio broadcasts transmitted by television and radio stations located in various States of the United States, and in the District of Columbia, having sufficient power to carry such broadcasts across state lines, for the purpose of inducing and which were likely to induce, directly or indirectly, the purchase of said drugs and have disseminated, and caused the dissemination of, advertisements concerning said drugs by various means, including but not limited to the aforesaid media, for the purpose of inducing and which were likely to induce, directly or indirectly, the purchase of said drugs in commerce.

PAR. 7. Typical of the statements and representations made in the advertisements, but not all inclusive thereof, are the following:

A. For Bayer Aspirin:

(1) To relieve a headache fast Bayer Aspirin's got the best help there is. Of all the leading pain relievers you see advertised, only Bayer is 100% aspirin. And Aspirin is what doctors recommend.

(2) I'm Ozzie Nelson. Here's something I'm passing along to *my* family. This booklet about pain relievers. Bayer tested its aspirin for quality against 220 other brands. The results? Bayer is superior. I also read about the latest report written by the American Medical Association Council on Drugs . . . Straight aspirin is preferred over other non-prescription pain relievers. Find out why . . . aspirin's the best pain reliever. And Bayer's the best aspirin.

(3) Has anyone ever improved on Bayer Aspirin? Made a faster Aspirin? A more effective Aspirin? Lots of people have tried. They took plain Aspirin. Made it bigger. Smaller. They buffered it. They added extra ingredients. They squeezed it. Squared it. Flavored it. Gummed it. Capsuled it. Fizzed it. Even tried spraying it . . . They did every thing—but improve it. Today there is still nothing faster . . . nothing more effective . . . than good old genuine Bayer Aspirin. It's pure Aspirin . . . not part Aspirin. It works wonders for headache, muscle pain, aches and fever of a cold. For just about anything that hurts.

(4) Would you like to see the inside story on all the major pain relievers you see advertised? Inside every single leading pain reliever is the same major ingredient . . . Aspirin . . . every one of those products relies chiefly on Aspirin. Surprised? Don't be . . . after all, Aspirin is the only pain reliever doctors overwhelmingly recommend for nearly every type of ache or pain. And did you know that Bayer is the only one of those pain relievers that makes all its own Aspirin? With care and experience no one else can match? That's why pure Bayer Aspirin, without Buffering or Caffeine or any other extra ingredient is the pain reliever for you.

(5) Deciding which pain reliever you should take can be like a game. Some talk about strength, some talk about speed, some talk about ingredients they don't name. But of all the leading pain relievers you see advertised, Bayer is the only one that is all Aspirin. And Aspirin is what doctors recommend.

(6) Bayer wants you to *know* about pain relievers . . . did you know that two Bayer Aspirin tablets bring all the pain relief power a headache can use? Did you know that Bayer without any additives is every bit as fast and effective in relieving pain as those products that have additives?

(7) Confused by claims? By shapes and sizes? By strange sounding ingredients? When you need fast relief from headache pain, don't forget this fact . . . Bayer is 100% Aspirin and Aspirin is the strongest pain reliever you can buy. No wonder Bayer works wonders.

(8) If you've ever heard that all aspirin's alike, here's something you should know. While it's true that the United States Pharmacopoeia does set standards for aspirin, Bayer surpasses these standards in many ways. For example, Bayer standards require complete tablet disintegration within thirty seconds. That's ten times faster than the accepted five-minute standard. It's one of the things that helps make Bayer fast and gentle.

(9) 1ST MAN: How come Bayer doesn't buffer its aspirin? BAYER MAN: There's really no need to. In relieving pain, buffered aspirin isn't any faster or gentler than Bayer. Yes.

(10) When hot weather makes you feel headachy, tense, irritable, two Bayer Aspirin and a short rest can help you feel better fast!

It happens to most of us on a hot, humid summer day, when the pressures of daily living mount up. By mid-afternoon we feel so headachy and edgy that the simplest chore, the smallest disturbance becomes an irritation. We're in no mood to enjoy life or the company of others.

Here's how to turn that mood around: just take two Bayer Aspirin for your headache, sit down for a few minutes and relax. You too will say, "Bayer works wonders." These few minutes can make a world of difference in the way you feel and act. You'll enjoy being with people, and they'll enjoy being with you.

Whenever you get headachy, tense and out of sorts on a hot summer afternoon, set aside a few minutes for Bayer Aspirin and a brief rest. Bayer is *pure* aspirin, not just *part* aspirin. Ask your pharmacist.

(11) Bayer recently tested its aspirin against 220 other brands. For purity, stability, speed of disintegration, Bayer was consistently better.

(12) I read about recent Bayer tests on aspirin. They tested for *quality,* for purity, for *freshness* against 220 other brands. The tests showed that Bayer makes the superior aspirin.

B. Bayer Aspirin for Children:

. . . You don't settle for any children's aspirin. You want the best. You want Bayer because no one makes aspirin like Bayer. No one purifies aspirin like Bayer. No one protects Aspirin like Bayer.

C. For Cope:

(1) Important studies made at the world's leading headache clinic show that for

relief of severe nervous tension headaches a combination of a pain reliever and a sedative provides greater relief than either medication alone. Of all the leading remedies you can buy for ordinary nervous tension headaches, only Cope combines a gentle relaxer with a powerful pain reliever for really effective relief. If you have chronic headaches, see your doctor. For the usual nervous tension headache get Cope.

(2) I get it on rainy days. I get it during rush hour. I get it when the boss looks over my shoulder. When the name of the pain is nervous tension headache, the name of the remedy is Cope. Because Cope gives you a powerful pain reliever plus a gentle relaxer.

D. For Vanquish:

(1) (3 tablets are shown with 1 caplet of Vanquish)

For your headache pain, here are your major choices. This leading extra strength product has no buffers. This leading buffered product has no extra strength. This leading pain reliever has strength but no buffers. Of all the leading pain relievers you can buy, only Vanquish gives you extra strength and gentle buffers. Vanquish. The choice. (Sterling Drug Inc.)

(2) When you get a headache we think you should take Vanquish. And we'll show you why in a head to head comparison. This is Vanquish. It gives you extra strength and gentle buffers. And it's the only leading pain reliever that does. This is a leading extra strength product. It has no buffers. And there are no buffers in this other extra strength product either. This leading buffered product comes without extra strength. We think your headache deserves extra strength and you deserve gentle buffers. (Sterling Drug Inc.)

(3) Vanquish is different. It gives you proven effectiveness of Aspirin as in this tablet plus extra medication as in these. But it also includes two gentle buffers . . . With Vanquish the only one. (Sterling Drug Inc.)

(4) Her headache is killing me. When she gets a pain in the head, it can be a big pain to me, so I give her Vanquish. Vanquish is strong medicine. Vanquish contains more pain relievers than the largest selling extra strength tablet . . . and it has gentle buffers. How's your headache, dear? Dit Dit Dit Dah . . . Vanquish is strong medicine. (Sterling Drug Inc., and Lois Holland Callaway, Inc.)

E. For Midol:

(1) Live Your Life . . . Relieved of Menstrual Distress. In the modern life you lead, there come the calm times, too. Strolling hand in hand. Reading together. Talking together. These are the precious, serene moments. And you let nothing interfere. Not even functional menstrual distress. How? With Midol. Because MIDOL contains:

An exclusive anti-spasmodic that helps STOP CRAMPS

Medically-approved ingredients that RELIEVE HEADACHE, LOW BACKACHE . . . CALM JUMPY NERVES . . .

Plus a special mood-brightener that gives you a real lift . . . gets you through the trying pre-menstrual period feeling calm and comfortable.

PAR. 8. Through the use of these advertisements, and others

similar thereto not specifically set out herein, it was represented directly or by implication:

A. By respondents Sterling Drug Inc., and Dancer-Fitzgerald-Sample, Inc., that it has been established that:

1. Bayer Aspirin is superior in terms of significant therapeutic effect to any other aspirin.

2. Bayer Children's Aspirin is superior in terms of significant therapeutic effect to any other children's aspirin.

3. A recommended dose of Cope is more effective for the relief of "nervous tension headache" pain than a recommended dose of any other non-prescription internal analgesic.

B. By respondent Sterling Drug Inc., that it has been established that:

1. A recommended dose of Vanquish is more effective for the relief of pain than a recommended dose of aspirin or buffered aspirin.

2. Because Vanquish contains "gentle buffers" it will result in less gastric discomfort than any non-prescription internal analgesic not containing buffers.

C. By respondents Sterling Drug Inc. and Lois Holland Callaway, Inc., that a recommended dose of Vanquish is more effective for the relief of pain than the largest selling "extra strength" tablet.

PAR. 9. In truth and in fact, none of said representations has been established, for reasons including, but not limited to, the existence of a substantial question, recognized by experts qualified by scientific training and experience to evaluate the safety and efficacy of such drugs, as to the validity of all such representations.

PAR. 10. Through the use of these advertisements, and others similar thereto not specifically set out herein, it was represented directly or by implication by respondents Sterling Drug Inc., and Dancer-Fitzgerald-Sample, Inc. that:

A. Bayer Aspirin is superior in terms of significant therapeutic effect to any other aspirin.

B. Bayer Children's Aspirin is superior in terms of significant therapeutic effect to any other children's aspirin.

PAR. 11. There existed, at the time of said representations, no reasonable basis for making the above representations, in that

respondents lacked competent and reliable scientific evidence sufficient to support such representations.

PAR. 12. Through the use of these advertisements, and others similar thereto not specifically set out herein, it was represented directly or by implication:

A. By respondents Sterling Drug Inc., and Dancer-Fitzgerald-Sample, Inc., that a recommended dose of Cope is more effective for the relief of "nervous tension headache" pain than a recommended dose of any other non-prescription internal analgesic.

B. By respondent Sterling Drug Inc., that:

1. A recommended dose of Vanquish is more effective for the relief of pain than a recommended dose of aspirin or buffered aspirin.

2. Because Vanquish contains "gentle buffers" it will result in less gastric discomfort than any non-prescription internal analgesic not containing buffers.

C. By respondents Sterling Drug Inc. and Lois Holland Callaway, Inc., that a recommended dose of Vanquish is more effective for the relief of pain than the largest selling "extra strength" tablet.

PAR. 13. There existed, at the time of said representations, a substantial question, recognized by experts qualified by scientific training and experience to evaluate the safety and efficacy of such drugs, as to the validity of such representations.

PAR. 14. Moreover, respondents made said representations without disclosing the existence of such a substantial question as to the validity of each representation. In light of the representations made, the existence of such a substantial question is a material fact, which, if known to consumers, would be likely to affect their consideration of whether or not to purchase such products. Thus, respondents have failed to disclose material facts.

PAR. 15. Through the use of the aforesaid advertisements and others similar thereto not specifically set out herein, it was represented directly or by implication:

A. By respondents Sterling Drug Inc. and Dancer-Fitzgerald-Sample, Inc. that a recommended dose of Bayer Aspirin relieves nervous tension, anxiety and irritability and improves the user's mood.

B. By respondents Sterling Drug Inc., and Dancer-Fitzgerald-Sample, Inc. that a recommended dose of Cope relieves nervous tension, anxiety and irritability and will enable persons to cope with the ordinary stresses of everyday life.

C. By respondent Sterling Drug Inc. that a recommended dose of Midol relieves nervous tension, stress, fatigue and depression and improves the user's mood.

PAR. 16. There existed at the time of said representations no reasonable basis for making the above representation in that respondents had no competent and reliable scientific evidence to support such representations.

PAR. 17. Through the use of the advertisements referred to in Paragraph Seven, sections (A) (2) (3) (4) (6) (7) and (9), (C), and (D) above it was represented directly or by implication:

A. By respondents Sterling Drug Inc., Dancer-Fitzgerald-Sample, Inc., that Bayer Aspirin is as effective for the relief of headache pain (including "nervous tension headache" pain) as, and will cause gastric discomfort no more frequently than, any other non-prescription internal analgesic, including Cope and Vanquish;

B. By respondents Sterling Drug Inc., and Dancer-Fitzgerald-Sample, Inc., that Cope is more effective for the relief of "nervous tension headache" pain than any other non-prescription internal analgesic, including Bayer Aspirin and Vanquish;

C. By respondent Sterling Drug Inc., that Vanquish is more effective for the relief of headache pain than any aspirin, including Bayer Aspirin, and will cause less gastric discomfort than any non-buffered internal analgesic, including Bayer Aspirin.

The representations referred to in sections (A), (B), and (C) above are mutually inconsistent. Respondents have made claims for a product that are inconsistent with contemporaneous claims for other products made by the same firm.

PAR. 18. Furthermore, in advertisements for Cope, respondents Sterling Drug Inc., and Dancer-Fitzgerald-Sample, Inc. referred to the results of tests or studies and represented, directly or by implication, that such tests or studies prove the claim that a recommended dose of Cope is more effective for the relief of "nervous tension headaches" than recommended doses of all other non-prescription internal analgesics.

PAR. 19. In truth and in fact, the tests or studies referred to do not prove the claim that a recommended dose of Cope is more effective for the relief of "nervous tension headaches" than recommended doses of all other non-prescription internal analgesics.

PAR. 20. Through the use of the advertisements referred to in Paragraph Seven, Sections A(11) and (12), and other similar thereto not specifically set out herein, respondents Sterling Drug Inc. and

Dancer-Fitzgerald-Sample, Inc. represented, directly or indirectly, that Bayer Aspirin has been tested against 220 other brands of aspirin for quality, purity, freshness, stability, and speed of disintegration, and that the results of the tests demonstrated that Bayer Aspirin is qualitatively superior to all of the other brands tested in all respects, and therapeutically superior to all of the other brands tested.

PAR. 21. In truth and in fact, the tests referred to do not demonstrate that Bayer Aspirin is qualitatively superior in all respects, including speed of disintegration, to all other aspirins tested. Moreover, these tests do not demonstrate that Bayer is therapeutically superior to all other brands because at the time of such representations there existed a substantial question, recognized by experts qualified by scientific training and experience to evaluate the safety and efficacy of such drug product, concerning the validity, significance or interpretation of such tests as related to such representation.

PAR. 22. Respondents Sterling Drug Inc. and Dancer-Fitzgerald-Sample, Inc. represented directly or by implication that Cope contained a unique formula in that it alone among non-prescription headache remedies contained both a pain reliever and an ingredient with sedative properties. In truth and in fact the ingredients referred to are aspirin and methapyrilene, both of which were available for non-prescription use in Excedrin PM. Therefore, the advertisements referred to in Paragraph Seven (C)(1) were and are misleading in a material respect.

PAR. 23. Respondents Sterling Drug Inc. and Lois Holland Callaway, Inc., marketed and advertised Vanquish without disclosing in the advertising for this product that it contains aspirin and caffeine. Aspirin and caffeine are well-known commonplace substances widely available in a variety of non-prescription products. Moreover, the use of aspirin or caffeine can be injurious to health and may cause undesirable side effects. Thus, respondents have failed to disclose in advertising a material fact, which if known to certain consumers would be likely to affect their consideration of whether or not to purchase such products.

PAR. 24. Furthermore, respondents Sterling Drug Inc. and Dancer-Fitzgerald-Sample, Inc. marketed and advertised Cope without disclosing in the advertising for this product that it contains aspirin and caffeine. Aspirin and caffeine are well-known commonplace substances widely available in a variety of non-prescription products. Moreover, the use of aspirin or caffeine can be injurious to health and may cause undesirable side effects. Thus, respondents

have failed to disclose in advertising a material fact, which if known to certain consumers would be likely to affect their consideration of whether or not to purchase such products.

PAR. 25. Furthermore, respondent Sterling Drug Inc. marketed and advertised Midol without disclosing in the advertising for this product that it contains aspirin and caffeine. Aspirin and caffeine are well-known commonplace substances widely available in a variety of non-prescription products. Moreover, the use of aspirin or caffeine can be injurious to health and may cause undesirable side effects. Thus, respondent has failed to disclose in advertising a material fact, which if known to certain consumers would be likely to affect their consideration of whether or not to purchase such products.

PAR. 26. Furthermore, in advertisements for Midol, respondents Sterling Drug Inc. and Thompson-Koch Company represented directly or by implication that the analgesic ingredients in Midol are other than ordinary aspirin and that the stimulant in Midol is other than caffeine.

PAR. 27. In truth and in fact, the analgesic ingredient in Midol is ordinary aspirin, and the stimulant in Midol is caffeine.

PAR. 28. The advertisements referred to in Paragraph Eight above were, and are, misleading in material respects, as alleged in Paragraphs Nine, Thirteen, Fourteen, Nineteen, Twenty-one, Twenty-two, Twenty-three, Twenty-four, Twenty-five, and Twenty-seven and constituted and now constitute false advertisements.

PAR. 29. The making of claims for a product that are inconsistent with contemporaneous claims for other products made by the same firm, as alleged in Paragraph Seventeen above, and the making of representations as alleged in Paragraphs Eleven, Thirteen, Fourteen, and Sixteen, constituted and now constitute unfair or deceptive acts or practices in commerce.

PAR. 30. The use by respondents of the aforesaid deceptive statements, representations, or claims, and the dissemination of the aforesaid false advertisements has had and now has, the capacity and tendency to mislead members of the consuming public into the erroneous and mistaken belief that said statements, representations, or claims were and are true and into the purchase of substantial quantities of said drugs of respondent Sterling Drug Inc. by reason of said erroneous and mistaken belief.

PAR. 31. In the course and conduct of its aforesaid business, and at all times mentioned herein, respondent Sterling Drug Inc. has been and now is in substantial competition in commerce, with corpora-

tions, firms and individuals in the sale of drug products of the general kind and nature as those sold by respondent.

In the course and conduct of its aforesaid business, and at all times mentioned herein, respondent Dancer-Fitzgerald-Sample, Inc. has been, and now is in substantial competition in commerce with other advertising agencies.

In the course and conduct of its aforesaid business, and at all times mentioned herein, respondent Lois Holland Callaway, Inc. has been, and now is in substantial competition in commerce with other advertising agencies.

PAR. 32. The aforesaid acts and practices of respondents, as herein alleged, including the dissemination of false advertisements, as aforesaid, were and are all to the prejudice and injury of the public and of respondents' competitors and constituted and now constitute unfair methods of competition in commerce and unfair or deceptive acts or practices in commerce, in violation of Sections 5 and 12 of the Federal Trade Commission Act.

DECISION AND ORDER

The Federal Trade Commission having issued a complaint which charges the above-named respondents with violation of the Federal Trade Commission Act; and

Respondent Dancer-Fitzgerald-Sample, Inc. ("Dancer") for the Commission having thereafter executed an agreement containing a consent order, an admission by respondent Dancer of all the jurisdictional facts set forth in the aforesaid complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent Dancer that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in 3.25 of its Rules, the Commission hereby makes the following jurisdictional findings, and enters the following order:

1. Respondent Dancer is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its principal office and place of business located at 347 Madison Ave., New York, New York.

2. The Federal Trade Commission has jurisdiction of the subject

matter of this proceeding and of respondent Dancer, and the proceeding against respondent Dancer is in the public interest.

ORDER

I

It is ordered, That respondent Dancer-Fitzgerald-Sample, Inc., a corporation, its successors and assigns, and respondents' officers, agents, representatives and employees directly or through any corporation, subsidiary, division or other device, forthwith cease and desist from:

A. Disseminating, or causing the dissemination of any advertisement by means of the United States mails or by any means in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act which:

1. Represents directly or by implication, in connection with the advertising, offering for sale, sale or distribution of Bayer Aspirin or any other product consisting of the same active ingredient in approximately equal amount, that Bayer Aspirin or such other product is superior in terms of significant therapeutic effect to any other aspirin unless such representation of superiority is true as applied to each and every brand of aspirin for which a comparison is made or implied.

2. Represents directly or by implication, in connection with the advertising, offering for sale, sale or distribution of Bayer Children's Aspirin, or any other product consisting of the same active ingredient in approximately equal amount, that Bayer Children's Aspirin or such other product is superior in terms of significant therapeutic effect to any other aspirin unless such representation of superiority is true as applied to each and every brand of aspirin for which a comparison is made or implied.

3. Represents directly or by implication, in connection with the advertising, offering for sale, sale or distribution of Cope, or any other product consisting of the same active ingredients in approximately equal amounts, that a recommended dose of Cope or such other product is more effective for the relief of nervous tension headaches than recommended doses of any other non-prescription analgesic.

4. Represents, directly or by implication, in connection with the advertising, offering for sale, sale or distribution of any non-prescription drug product, that any non-prescription drug product has a

unique combination of ingredients when the claimed unique combination is contemporaneously available, regardless of proportion, in other non-prescription drug products unless respondent can establish that it neither knew, nor had reason to know, nor upon reasonable inquiry could have known of such other non-prescription drug product.

5. Fails to disclose that Cope contains aspirin and caffeine.

B. Disseminating or causing the dissemination of any advertisement by any means, which contains statements which are inconsistent with, negate, or contradict any disclosures required by Paragraph A(5) above, or in any way obscure the meaning of such disclosures;

C. Disseminating, or causing the dissemination of, any advertisement by any means, for the purpose of inducing or which is likely to induce, directly or indirectly, the purchase of any of the products named in Paragraph A above in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, which contains any of the representations prohibited in Subparagraphs A(1) through A(4) above; or which fails to disclose the disclosures required in Subparagraph A(5) above;

D. Representing that aspirin alone relieves nervous tension, anxiety or irritability or will improve the user's mood;

E. Representing that a recommended dose of Cope, or any other product consisting of the same active ingredients in approximately equal amounts, relieves nervous tension, anxiety or irritability or will enable persons to cope with the ordinary stresses of everyday life;

F. Making any statement or representation, directly or by implication, concerning any product which is inconsistent with a contemporaneous claim made by respondent for any other product manufactured or distributed by the same advertiser, either directly or through any corporation, subsidiary, division or other device.

G. Representing directly or by implication, in connection with the advertising, offering for sale, sale or distribution of any non-prescription drug product that any claim is proved by one or more tests or studies when such tests do not prove such claims unless respondent can establish that it neither knew nor had reason to know, nor upon reasonable inquiry could have known, that such tests do not prove such claims.

II

It is ordered, That respondent Dancer-Fitzgerald-Sample, Inc., a

corporation, its successors and assigns, and respondents' officers, agents, representatives and employees directly or through any corporation, subsidiary, division or other device, in connection with the advertising, offering for sale, sale or distribution of any non-prescription drug product do forthwith cease and desist from:

A. Disseminating, or causing the dissemination of, any advertisement by means of the United States mails or by means in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, which represents, directly or by implication, that a claim concerning the performance, effectiveness, or freedom from side effects of such product has been established, when there exists a substantial question, recognized by experts qualified by scientific training and experience to evaluate the safety and efficacy of such drug products, as to the validity of such claim, unless respondent can establish that it neither knew nor had reason to know, nor upon reasonable inquiry could have known, of the existence of such substantial question;

B. Making any statements or representations, directly or by implication, concerning the performance, effectiveness, or freedom from side effects of such product, unless at the time of such representations, respondents have competent and reliable scientific evidence to support such representations.

III

It is ordered, That respondent Dancer-Fitzgerald-Sample, Inc., a corporation, its successors and assigns, and respondents' officers, agents, representatives and employees directly or through any corporation, subsidiary, division or other device, in connection with the advertising, offering for sale, sale or distribution of any non-prescription drug product do forthwith cease and desist from:

A. Disseminating, or causing the dissemination of, any advertisement by means of the United States mails or by any means in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, which fails to disclose that the product contains aspirin or caffeine, if such is the case; *provided, however,* that a disclosure of aspirin content shall be unnecessary where the trademark or name contains the term "Aspirin;"

B. Disseminating, or causing the dissemination of, any advertisement by any means, which contains statements which are inconsistent with, negate or contradict any disclosures required by Para-

graph A above, or in any way obscure the meaning of such disclosures;

C. Making any representation, directly or by implication, concerning the performance, effectiveness, or freedom from side effects of such product, when there exists a substantial question, recognized by experts qualified by scientific training and experience to evaluate the safety and efficacy of such drug products, as to the validity of such representation unless respondent can establish that it neither knew nor had reason to know, nor upon reasonable inquiry could have known, of the existence of such substantial question.

IV

Provided, however, that Paragraphs II(A) and III(C) of this Order shall not take effect or be binding unless or until an order provision embodying the "Standard" set forth in Paragraphs II(A) and III(C), or any modification thereof, becomes final with respect to Sterling Drug Inc., co-respondent joined in the complaint issued in Docket 8919. *Provided further,* that should said order against Sterling Drug Inc., contain a standard different or modified in any respect from the "Standard" set forth in said paragraphs, both parties agree to a reopening and modification of these paragraphs for the sole purpose of incorporating said modification into these paragraphs. For the purpose of this Paragraph IV the "Standard" shall mean "when there exists a substantial question recognized by experts qualified by scientific training and experience to evaluate the safety and efficacy of such non-prescription internal analgesic product".

Provided further, that the defense of "neither knew nor had reason to know, nor upon reasonable inquiry could have known," as set forth in Paragraphs II(A) and III(C) of this Order shall not be revised or modified or otherwise affected, even though the "Standard" finally utilized is different or modified in any respect from the "Standard" set forth in said paragraphs.

Provided further, that should said order against Sterling Drug Inc., with respect to the prohibitions contained in Paragraphs II(A) and III(C) of this Order, prohibit only representations as to the comparative performance, comparative effectiveness and comparative freedom from side effects, both parties agree to a reopening and modification of these paragraphs for the sole purpose of incorporating said modification into these paragraphs.

V

Provided further, that Paragraphs III(A) and III(B) of this Order

shall not take effect or be binding unless or until an order provision requiring the disclosure of aspirin or caffeine content becomes final with respect to Sterling Drug Inc. in Docket 8919.

Provided further, that nothing contained in this Order shall in any way limit respondent's right to move for a reopening of the Order under the Rules of the Commission and request a modification thereof in accordance with the provisions of those Rules.

VI

It is further ordered, That respondent corporation shall forthwith distribute a copy of this Order to each of its operating divisions.

It is further ordered, That respondent notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondent such as dissolution, assignment or sale, resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other changes in the corporation which may affect compliance obligations arising out of the Order.

It is further ordered, That respondent shall, within sixty (60) days and at the end of six (6) months after the effective date of the Order served upon it, file with the Commission a report, in writing, signed by respondent, setting forth in detail the manner and form of its compliance with the Order to cease and desist.

Commissioner Pitofsky did not participate.

IN THE MATTER OF

BOB RICE FORD, INC., ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION AND MAGNUSON-MOSS WARRANTY ACTS

Docket C-3026. Complaint, July 1, 1980—Decision, July 1, 1980

This consent order requires, among other things, a Boise, Idaho seller of new and used motor vehicles and its corporate officer to make the text of written warranties readily available to prospective buyers and prominently display signs advising consumers of such availability. Written warranties must include all statutorily required information, and limited warranties so designated. Respondents are also required to post signs stating that all warranties are not the same and that comparisons should be made prior to purchase. All relief available to purchasers under state laws must be provided; and affected customers, in instances where implied warranties were improperly waived, notified of their implied warranty rights. Further, the order bars respondents from raising any defenses pertaining to a disclaimer of implied warranties in suits brought by motor vehicle purchasers who were issued written limited warranties disclaiming implied warranties. Additionally, respondents are required to instruct their employees as to their statutory obligations, and maintain a surveillance program designed to ensure compliance with the provisions of the order.

Appearances

For the Commission: *Dennis D. McFeely.*

For the respondents: *Paul T. Baird,* Boise, Idaho.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, as amended, and of the Magnuson-Moss Warranty—Federal Trade Commission Improvement Act ("Warranty Act"), the implementing Rules concerning the Disclosure of Written Consumer Product Warranty Terms and Conditions ("Disclosure Rule") (16 C.F.R. 701 (1977)) and the Availability of Written Warranty Terms ("Pre-Sale Rule") (16 C.F.R. 702 (1977)) duly promulgated on December 31, 1975 pursuant to Title I, Section 109 of the Warranty Act (15 U.S.C. 2309), and by virtue of the authority vested in it by said Acts, the Federal Trade Commission, having reason to believe that Bob Rice Ford, Inc., a corporation, and Robert L. Rice, individually and as an officer of said corporation, hereinafter sometimes referred to as respondents, have violated the provisions of said Acts, the Pre-Sale Rule and the

Disclosure Rule, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. The present tense as used herein includes the past tense.

PAR. 2. Respondent Bob Rice Ford, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Idaho. Its principal office and place of business is located at 3150 Main St., Boise, Idaho.

Respondent Bob L. Rice is an officer of said corporation. He formulates, directs and controls the policies, acts and practices of said corporation, and his address is the same as that of Bob Rice Ford, Inc.

PAR. 3. Respondents have been, and are now, engaged in the advertising, offering for sale, and sale of new and used automobiles and trucks to the public.

PAR. 4. In the course and conduct of their business, respondents offer for sale and sell to consumers, consumer products distributed in commerce as "consumer product," "consumer," "distributed in commerce," and "commerce," are defined by Sections 101(1), 101(3), 101(13) and 101(14), respectively, of the Warranty Act. Respondents are, therefore, suppliers as "supplier" is defined by Section 101(4) of the Warranty Act.

COUNT 1

PAR. 5. Alleging violation of the Warranty Act and Section 5 of the Federal Trade Commission Act, the allegations of Paragraphs One through Four are incorporated by reference herein as if fully set forth verbatim.

PAR. 6. Respondents, in the course and conduct of their business, have offered and sold automobiles and other consumer products manufactured after July 4, 1975 costing the consumer in excess of $15.00, many of which are warranted by the manufacturer. Respondents are therefore sellers as "seller" is defined in Section 702.1(e) of the Pre-Sale Rule.

PAR. 7. In connection with the offering for sale and sale of automobiles and other consumer products manufactured after January 1, 1977, respondents have failed, as required by Section 702.3(a) of the Pre-Sale Rule, to make the text of any written warranty available for prospective buyers' review prior to sale.

PAR. 8. Respondents' failure to comply with the Pre-Sale Rule as

described in Paragraphs Six and Seven of this complaint is a violation of the Warranty Act, and, pursuant to Section 110(b) of the Warranty Act, is an unfair or deceptive act or practice in violation of Section 5 of the Federal Trade Commission Act, as amended.

COUNT 2

PAR. 9. Alleging violation of the Warranty Act and Section 5 of the Federal Trade Commission Act, the allegations of Paragraphs One through Four are incorporated by reference herein as if fully set forth verbatim.

PAR. 10. In the course and conduct of its business, respondents provide to purchasers of used automobiles and trucks manufactured after July 4, 1975 a written limited warranty covering the engine, transmission, rear axle, brake system, and electrical system. Respondents are therefore warrantors as "warrantor" is defined by Section 101(5) of the Warranty Act.

PAR. 11. In connection with the respondents' providing of written warranties, respondents have failed to designate the warranty as a "Limited Warranty" as required by Section 103 of the Warranty Act.

PAR. 12. Respondents' failure to properly designate their warranty is a violation of Section 103 of the Warranty Act, and, pursuant to Section 110(b) of the Warranty Act, is an unfair or deceptive act or practice in violation of Section 5 of the Federal Trade Commission Act, as amended.

COUNT 3

PAR. 13. Alleging violation of the Warranty Act and Section 5 of the Federal Trade Commission Act, the allegations of Paragraphs One through Four and Paragraph Ten are incorporated by reference herein as if fully set forth verbatim.

PAR. 14. In written warranties provided to purchasers of used automobiles and trucks manufactured after January 1, 1977 respondents have failed to clearly and conspicuously disclose in a single document in simple and readily understood language the following statements:

A. This warranty gives you specific legal rights, and you may also have other rights which vary from state to state.

B. Some states do not allow the exclusion or limitation of incidental or consequential damages, so the above limitation or exclusion may not apply to you.

Failure to include these statements violates Section 701.3 of the Disclosure Rule.

PAR. 15. Respondents' failure to comply with the Disclosure Rule as described in Paragraph Fourteen of this complaint is a violation of the Warranty Act, and, pursuant to Section 110(b) of the Warranty Act, is an unfair or deceptive act or practice in violation of Section 5 of the Federal Trade Commission Act, as amended.

COUNT 4

PAR. 16. Alleging violation of the Warranty Act and Section 5 of the Federal Trade Commission Act, the allegations of Paragraphs One through Four and Paragraph Ten are incorporated by reference herein as if fully set forth verbatim.

PAR. 17. While providing written warranties to purchasers, of used automobiles and trucks manufactured after July 4, 1975, respondents have, with respect to those same purchasers, disclaimed all implied warranties (including the implied warranties of merchantability and fitness for a particular use) arising under state law and otherwise available to purchasers of respondents' automobiles and trucks.

PAR. 18. Respondents' disclaimer of the implied warranties as described in Paragraph Seventeen of this complaint is a violation of Section 108 of the Warranty Act, and, pursuant to Section 110(b) of the Warranty Act, is an unfair or deceptive act or practice in violation of Section 5 of the Federal Trade Commission Act, as amended.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondents named in the caption hereof, and the respondents having been furnished thereafter with a copy of a draft of complaint which the Seattle Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondents with violation of the Federal Trade Commission Act; and the Magnuson-Moss Warranty Act.

The respondents, their attorneys, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondents of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondents that the law has been

violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Federal Trade Commission having initiated an investigation of certain acts and practices of Bob Rice Ford, Inc., a corporation, and Robert L. Rice, individually and as an officer of said corporation, and it now appearing that said corporation, and Robert L. Rice, individually and as an officer of said corporation, hereinafter sometimes referred to as proposed respondents, are willing to enter into an agreement containing an order to cease and desist from the use of the acts and practices being investigated,

It is hereby agreed, by and between Bob Rice Ford, Inc., by its duly authorized officer, Robert L. Rice, individually and as an officer of said corporation, and counsel for the Federal Trade Commission that:

1. Proposed respondent Bob Rice Ford, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Idaho with its principal office and place of business located at 3150 Main St., Boise, Idaho.

Proposed respondent Robert L. Rice is an officer of said corporation. He formulates, directs and controls the policies, acts and practices of said corporation, and his address is the same as that of said corporation.

2. Proposed respondents admit all the jurisdictional facts set forth in the draft of complaint here attached.

3. Proposed respondents waive:

(a) Any further procedural steps;

(b) The requirement that the Commission's decision contain a statement of findings of fact and conclusions of law; and

(c) All rights to seek judicial review or otherwise to challenge or contest the validity of the order entered pursuant to this agreement.

4. This agreement shall not become a part of the official record of the proceeding unless and until it is accepted by the Commission. If this agreement is accepted by the Commission it, together with the draft of complaint contemplated thereby and related material pursuant to Rule 2.34, will be placed on the public record for a period of sixty (60) days and information in respect thereto publicly released. The Commission thereafter may either withdraw its acceptance of this agreement and so notify the proposed respondents, in which event it will take such action as it may consider appropriate, or issue and serve its complaint (in such form as the circumstances may require) and decision, in disposition of the proceeding.

5. This agreement is for settlement purposes only and does not

constitute an admission by respondents that the law has been violated as alleged in the draft of complaint here attached.

6. This agreement contemplates that, if it is accepted by the Commission, and if such acceptance is not subsequently withdrawn by the Commission pursuant to the provisions of Section 2.34 of the Commission's Rules, the Commission may, without further notice to proposed respondents, (1) issue its complaint corresponding in form and substance with the draft of complaint here attached and its decision containing the following order to cease and desist in disposition of the proceeding, and (2) make information public in respect thereto. When so entered, the order to cease and desist shall have the same force and effect and may be altered, modified or set aside in the same manner and within the same time provided by statute for other orders. The order shall become final upon service. Delivery by the U.S. Postal Service of the complaint and decision containing the agreed-to order to proposed respondents' address as stated in this agreement shall constitute service. Proposed respondents waive any rights they may have to any other manner of service. The complaint may be used in construing the terms of the order, and no agreement, understanding, representation, or interpretation not contained in the order or the agreement may be used to vary or contradict the terms of the order.

7. Proposed respondents have read the proposed complaint and order contemplated hereby. They understand that once the order has been issued, they will be required to file one or more compliance reports showing that they have fully complied with the order, and that they may be liable for civil penalties in the amount provided by law for each violation of the order after it becomes final.

ORDER

I. Definitions

A. "Warranty Act" means the Magnuson-Moss Warranty—Federal Trade Commission Improvement Act (15 U.S.C.2301, *et seq.*).

B. The definition of terms contained in Section 101 of the Warranty Act and in Rules 701 and 702 promulgated thereunder (16 C.F.R. 701.1, 702.1) as presently defined and as may be amended hereafter, shall apply to the terms of this order.

C. With respect to new automobiles and trucks, "display area" means a prominent location in the showroom.

II.

It is ordered, That respondent Bob Rice Ford, Inc., a corporation, its successors and assigns, and its officers, and Robert L. Rice, individually and as an officer of said corporation, and respondents' agents, representatives and employees, directly or indirectly through any corporation, subsidiary, division or other device, in connection with the advertising, offering for sale, and sale of automobiles or other consumer products:

A. Shall, with respect to written warranties on new cars and other new consumer products, make available to the consumer prior to sale through utilization of a binder system as specified in 16 C.F.R. 702.3(a)(1)(ii), as presently written and as may be amended hereafter, the text of any written warranties offered or provided by respondents or the manufacturers of automobiles and consumer products sold by respondents. In utilizing any such binder or binders respondents shall:

1. provide prospective buyers with ready access thereto; and
2. a. display such binder(s) in a manner reasonably calculated to elicit the prospective buyers' attention; or

b. i. make such binder(s) available to prospective buyers on request; and

ii. place signs reasonably calculated to elicit the prospective buyers' attention in prominent locations within the display area, advising such prospective buyers of the availability of the binder(s), including instructions for obtaining access; and

3. index such binder(s) according to product or warrantor; and
4. clearly entitle such binder(s) as "Warranties" or other similar title.

Provided, however, that with respect to written warranties on new cars, it shall be deemed compliance with this paragraph if respondents display the text of any written warranties offered on new cars in the showroom in a manner reasonably calculated to elicit prospective buyers' attention, employing any means authorized by 16 C.F.R. 702.3(a)(1)(i) or (iv), as presently written and as may be amended hereafter. In such instance, the sign required by Paragraph III(A) shall be amended by inserting, in lieu of Line 3, the phrase "The warranty on new cars is posted in this showroom," and inserting, in lieu of Line 4, the phrase "There is also a warranty binder for parts and accessories."

B. Shall clearly and conspicuously display the text of each written warranty offered by respondents for used motor vehicles on a

window of each warranted vehicle; *provided,* that in the event the Federal Trade Commission issues a final Trade Regulation Rule establishing requirements which make compliance with this paragraph impossible, or which requires disclosure of warranty terms on window forms, then this paragraph will be null and void.

III.

It is further ordered, That respondents:

A. Post, in a prominent location in the showroom, a sign, at least 36 inches wide by 48 inches high and reasonably calculated to elicit prospective buyers' attention, which contains a verbatim reproduction of the following language:

IMPORTANT!
NOT ALL WARRANTIES ARE THE SAME
Compare warranties before you buy
There is a warranty binder in this showroom
If you can't find it, ask for it
Check for these things:
Full or Limited:
What costs are covered?
What do *you* have to do?
Are all parts covered?
How long does the warranty last?

B. Post, in a prominent location in the used car sales office lobby, a sign, at least 36 inches wide by 48 inches high and reasonably calculated to elicit prospective buyers' attention, which contains a verbatim reproduction of the following language:

IMPORTANT!
NOT ALL WARRANTIES ARE THE SAME
Compare warranties before you buy
Warranties (when given) are on the windows of used cars
If you don't see it, ask about it
Check for these things:
Full or Limited:
What costs are covered?
What do *you* have to do?
Are all parts covered?
How long does the warranty last?

C. The signs required by Paragraphs III.A. and B. shall be posted for a period of not less than three years from the effective date of this order. The language in such signs shall be unencumbered by other written or visual matter, shall be spaced, indented and punctuated

336-345 O - 81 - 3

as indicated in Paragraphs III.A. and B. above, and shall be printed in black against a solid white background, as follows:

1. The title of each sign shall be the word "Important" and shall be printed in capital letters in 4-inch boldface type followed by an exclamation mark.
2. The next phrase shall be printed on a separate line in capital letters and in 3-inch medium face type.
3. The next three phrases shall be printed on separate lines and in 3-inch medium face type.
4. Each succeeding phrase shall be printed on a separate line and in 2-inch medium face type.
5. The word "Important!" and each phrase shall be at least one inch from every other phrase.

IV.

It is further ordered, That respondents in connection with the advertising, offering for sale, and sale of automobiles and other consumer products shall clearly and conspicuously designate written warranties offered by said respondents as required by Section 103 of the Warranty Act. If a written warranty is given which does not meet the standards set forth in Section 104 of the Warranty Act:

A. The warranty shall be titled "Limited Warranty"; and
B. The title shall be printed in capital letters in 44-point boldface type.

V.

It is further ordered, That respondents in connection with the offering of written warranties on automobiles and other consumer products shall clearly and conspicuously disclose in a single document in simple and readily understood language, the following items of information:

A. The identity of the party or parties to whom the written warranty is extended, if the enforceability of the written warranty is limited to the original consumer purchaser or is otherwise limited to persons other than every consumer owner during the term of the warranty;
B. A clear description and identification of products, or parts, or characteristics, or components or properties covered by and, where necessary for clarification, excluded from the warranty;
C. A statement of what the warrantor will do in the event of a

defect, malfunction or failure to conform with the written warranty, including the items or services the warrantor will pay for or provide, and, where necessary for clarification, those which the warrantor will not pay for or provide;

D. The point in time or event on which the warranty term commences, if different from the purchase date, and the time period or other measurement of warranty duration;

E. A step-by-step explanation of the procedure which the consumer should follow in order to obtain performance of any warranty obligation, including the persons or class of persons authorized to perform warranty obligations. This includes the name(s) of the warrantor(s), together with: the mailing address(es) of the warrantor(s), and/or the name or title and the address of any employee or department of the warrantor responsible for the performance of warranty obligations, and/or a telephone number which consumers may use without charge to obtain information on warranty performance;

F. Information respecting the availability of any informal dispute settlement mechanism that complies with 16 C.F.R. 703 (1977);

G. Any limitations on the duration of implied warranties, disclosed on the face of the warranty as provided in Section 108 of the Warranty Act, accompanied by the following statement:

Some states do not allow limitations on how long an implied warranty lasts, so the above limitation may not apply to you.

H. Any exclusions of or limitations on relief such as incidental or consequential damages, accompanied by the following statement, which may be combined with the statement required in subparagraph G above:

Some states do not allow the exclusion or limitation of incidental or consequential damages, so the above limitation or exclusion may not apply to you.

I. A statement in the following language:

This warranty gives you specific legal rights, and you may also have other rights which vary from state to state.

VI.

It is further ordered, That respondents, in connection with the advertising, offering for sale, and sale of automobiles or other consumer products in instances where respondents either provide a written warranty to the consumer with respect to such consumer product, or, at the time of sale or within 90 days thereafter, enter

into a service contract with the consumer which applies to such consumer product, shall:

A. Not disclaim or modify, except as permitted by Section 108(b) of the Warranty Act, any implied warranty with respect to a consumer product;

B. Not limit the duration of any implied warranty with respect to a consumer product unless:

1. any written warranty is clearly and conspicuously designated a "Limited Warranty"; and

2. the limitation is for a period of time at least as long as the duration of any written warranty provided by respondents with respect to the product; and

3. the duration of the written warranty is for a reasonable duration; and

4. the limitation is conscionable, is set forth in clear and unmistakable language, and is prominently displayed on the face of the warranty.

VII.

It is further ordered, That respondents shall:

A. Not raise any defenses pertaining to a disclaimer, limitation or modification of implied warranties in any case, suit or claim brought or made against respondents by consumers who have purchased any of respondents' warranted motor vehicles manufactured after July 4, 1975 and who were issued a written limited warranty disclaiming implied warranties;

B. Provide, in good faith, all consumers with all relief available to them under applicable Idaho state laws, if:

1. said consumers purchased any of respondents' warranted motor vehicles manufactured after July 4, 1975 and were issued a used car owner security plan attempting to disclaim implied warranties; and

2. if said motor vehicles did not comply with all of the implied warranties;

C. Notify all consumers who have purchased any of respondents' warranted motor vehicles manufactured after July 4, 1975 and were issued a used car owner security plan which attempted to disclaim implied warranties, by mailing to each such consumer within 60 days of the effective date of this order at the customer's last residence

address known to respondents, the notice set forth in Appendix A of this order. If the notice is returned undelivered, the return envelope shall be retained and the notice is to be sent to the customer's last employment address known to respondents or to the address of a co-signer, relative or other person through whom the customer may be reached.

VIII.

It is further ordered, That:

A. Respondents deliver a copy of this order to cease and desist to all present and future employees, salespersons, agents, independent contractors, and other representatives of respondents engaged in the sale of automobiles or consumer products on behalf of respondents, and secure a signed statement acknowledging receipt of the order from each such person.

B. Respondents instruct all present and future employees, salespersons, agents, independent contractors, and other representatives of respondents, engaged in the sale of automobiles or other consumer products on behalf of respondents, as to their specific obligations and duties under the Warranty Act, all present and future implementing Rules promulgated under the Act and this order including but not limited to:

1. instructions as to the availability and location of warranty information;
2. instructions as to the nature of and differences among full warranties, limited warranties, and service contracts.

C. Respondents institute a program of continuing surveillance to reveal whether respondents and respondents' employees, salespersons, agents, independent contractors, or other representatives are in compliance with this order.

D. Respondents maintain complete records for a period of not less than three (3) years from the date of the incident, of any written or oral information received which indicates the possibility of a violation of this order by any of respondents' employees, salespersons, agents, independent contractors, or other representatives. Any oral information received indicating the possibility of a violation of the order shall be reduced to writing, and shall include the name, address and telephone number of the informant, the name and address of the individual involved, the date of the communication and a brief summary of the information received. Such records shall

be available upon request to representatives of the Federal Trade Commission during normal business hours upon reasonable advance notice.

E. Respondents maintain, for a period of not less than three (3) years from the effective date of this order, complete business records including customer sale folders to be furnished upon request to the staff of the Federal Trade Commission, relating to the manner and form of their continuing compliance with all the terms and provisions of this order.

F. The corporate respondent named herein notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondent such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporate respondent which may affect compliance obligations arising out of this order.

G. For a period of five years, the individual respondent named herein promptly notify the Commission of the discontinuance of his present business or employment and/or of his affiliation with a new business or employment.

H. Respondents herein shall within sixty (60) days after service upon them of this order, file with the Commission a report, in writing, setting forth in detail the manner and form in which they have complied with this order.

Appendix A

[Date]

[Name and Address of Consumer]

Dear [Name of Consumer]:

Some time ago you bought from us a used car or truck made after July 3, 1975. We gave you our "Ford Dealer Used Car Owner Security Plan." It said that for a certain time after you bought your car or truck, we would give you a discount on certain repairs.

We have learned that this plan is a warranty under federal law. This means we should not have disclaimed any implied warranties.

In fact, you do have an implied warranty of merchantability. This means that the car or truck you purchased must have been fit for ordinary use. Furthermore, if you relied on any claim made by us at the time you purchased the vehicle that it was fit for a particular purpose, you have a warranty of fitness for a particular purpose. The vehicle must fit the purpose we claimed it would fit. The law of the State of Idaho gives you four years to enforce these implied warranties.

We feel we have lived up to our "Security Plan." It said we would make repairs at a discount for a certain time after you bought your car or truck. If you feel we have not lived up to the other warranties shown above, you have a legal right to them, even though we disclaimed them in error. If you have any questions, please call us at 342-6811.

Please excuse these mistakes in our warranty.

Sincerely,

Bob Rice Ford, Inc.
A. W. Baril, Vice President &
General Manager

IN THE MATTER OF

FORD MOTOR COMPANY, ET AL.

MODIFYING ORDER IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket 9073. Decision, March 29, 1979—Modifying Order, July 3, 1980

This order changes some of the order provisions in an order to cease and desist issued against a Detroit, Mich. manufacturer of motor vehicles March 29, 1979, 93 F.T.C. 402, 44 FR 25630. In an effort to insure evenhandedness in requirements in similar cases issued against competitors, the Commission is modifying the order provisions to meet those in a provisionally accepted order against General Motors Corporation. The Commission has eliminated the references to the State of Louisiana in Paragraphs I.J and II.F; redefined the meaning of "allowable expenses" in Paragraph I.L; and removed the requirement that respondent submit summary reports of certain required audits to the agency. The order now requires simply the preparation and maintenance of such audit summary reports.

ORDER REOPENING AND MODIFYING CONSENT ORDER

On March 29, 1979, the Commission issued a Decision and Order against respondents Ford Motor Company and Ford Motor Credit Company,[1] in connection with the extension and enforcement of motor vehicle retail credit obligations and the disposition of repossessed motor vehicles. There is now before the Commission a Request by the Ford respondents (filed May 30, 1980, and amended June 10, 1980) for reopening and modification of that Order pursuant to Section 2.51 of the Commission's Rules of Practice, 16 C.F.R. 2.51.

The Order required Ford to establish and provide to all dealers, as part of the Ford Manual of Dealer Accounting Procedure (binding on all Ford dealers), a system for determining repossession surpluses and for accounting for such surpluses and for any deficiencies sought on repossessed vehicles. It required also that Ford conduct a series of field audits to verify whether its dealers are in fact adhering to that system.

Order Paragraph I.J defines "disposition" of a repossessed vehicle to include its sale or lease, but not transactions subsequent to judicial sales in Louisiana.[2] In accordance with the latter aspect,

[1] 93 F.T.C. 402. The Order was modified on February 16, 1980, [45 FR 22020; 95 F.T.C. 349] at the behest of the Ford respondents and without objection by the Commission's staff, in a single subparagraph unaffected by the Request discussed herein.

[2] The full text of Paragraph I.J is as follows:

J. "Disposition" or "dispose" refers to a dealership's sale or lease of a repossessed vehicle previously sold by that dealership and returned to it by or for a financing institution pursuant to a repurchase agreement. Such sale or lease includes only transactions with an independent third party; *i.e.*, it does not include a sale

(Continued)

Paragraph II.F limits the coverage of the repossession accounting system as follows:

F. The accounting system shall not apply to sales of repossessed vehicles subsequent to judicial sales in Louisiana.

The Order further provides, in Paragraph I.L, that the following expenses, among others, may be deducted as "allowable" in dealers' determination of surpluses and of deficiencies upon which collection is attempted:

* * * * * * *

7. sales commissions paid for actual participation in the sale of the particular vehicle, computed at a rate no higher than for a similar, nonrepossessed vehicle and excluding portions of commissions attributable to the selling of service contracts, separately priced warranties, financing or insurance;

* * * * * * *

10. expenses for telephone calls and postage incurred in arranging for the repossession, holding, transportation, reconditioning and resale of the vehicle.

As to the Ford-conducted audits, Paragraph IV.H requires that "[w]ithin sixty days after completion of each audit of a dealership . . . Ford shall:

1. submit to the Federal Trade Commission a summary report of the audit for that dealership, containing . . . [seven specified categories of information and/or documentation]."

The current Ford Request relies on various manifestations of Commission policy in favor of evenhanded treatment of similarly situated business entities. As amended, the Request asks that Paragraphs I.J, II.F, I.L and IV.H.1 of the March 1979 Order be modified to "conform" in certain respects to a consent order agreement with General Motors Corporation, et al., accepted subject to public comment on March 5, 1980 (Docket 9074, 45 FR 14870, March 7, 1980). Specifically, Ford seeks elimination of the "in Louisiana" limitation from Paragraphs I.J and II.F; clarification that expenses incident to any proper disposition (i.e., a sale *or* lease, rather than just a sale) may be deducted as "allowable" in determining the amount of any surplus or deficiency; and provision that these expenses may include costs of certain fringe benefits

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or lease to the financing institution, the dealership or their representatives, or to a person or firm liable under a guaranty, endorsement, or repurchase agreement covering the repossessed vehicle. Disposition or dispose shall not refer to the repurchase of a repossessed vehicle by a dealership pursuant to a repurchase agreement, or refer to a sale subsequent to a judicial sale in Louisiana.

incurred in connection with payment of sales commissions, certain other certain necessary photocopying and communication expenses, and amounts paid specifically to insure the repossessed vehicle while in the dealer's possession.

Because the audit process incorporated in the *General Motors* consent order requires preparation and maintenance of a summary report of each dealership audit (*GM* ¶¶ IV.A.3 and IV.B) but not their automatic submittal to the Commission, Ford asks that Paragraph IV.H.1 be modified to require only preparation and not routine submission (to the Commission) of its individual dealership audit reports. Ford notes that such reports would still be available for review by Commission representatives upon request, under the general-recordkeeping provision of the Order (Paragraph VIII.A). In addition, Ford undertakes to submit two statistical reports to the Commission during the conduct of each sample audit, to provide Commission staff with interim overviews while the audit process is still ongoing.

The Commission's staff concurs in all of the modifications proposed in Ford's Request, as amended.[3] However, with the exception of the changes to Paragraph I.L the staff does not agree with Ford's contention that the modifications are within the scope of Paragraph VII.B (which confers upon Ford a right to have any provision conformed, as necessary and appropriate, to a corresponding provision of any final order in Dockets 9072–74 which prescribes a less restrictive standard on certain enumerated subjects). Because the Commission has decided to grant all aspects of Ford's amended Request,[4] as an exercise of sound discretion—in the interest of prompt evenhandedness rather than contingent on finality of the *General Motors* order—it is unnecessary to make a determination as to whether the requested modifications of Paragraphs I.J, II.F and IV.H.1 fall within the scope and operation of Paragraph VII.B.

Therefore, the Commission being of the opinion that the public interest will be served by modifying the Order as requested, at this time,

It is ordered, That Docket 9073 be, and it hereby is, reopened for the limited purpose of effecting the following changes.

It is further ordered, That Paragraphs I.J and II.F of the Order be modified by eliminating references to Louisiana, so that the last sentence of Paragraph I.J will read:

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[3] The Commission notes that no comments were filed on these aspects of the *General Motors* consent order during its sixty days on the public record, and that none have been filed on Ford's Request.

[4] In implementation of its proposed modifications to Paragraph I.L, Ford has submitted detailed revisions of certain portions of its Manual of Dealer Accounting Procedure. Pending staff review of these materials, the Commission expresses no view at this time as to their compliance with the modified provisions.

Disposition or dispose shall not refer to the repurchase of a repossessed vehicle by a dealership pursuant to a repurchase agreement, or refer to a sale subsequent to a judicial sale.

and Paragraph II.F will read:

F. The accounting system shall not apply to sales of repossessed vehicles subsequent to judicial sales.

It is further ordered, That Paragraph I.L of the Order be modified in its preamble and in certain indicated subparagraphs, and by addition of a new subparagraph 11, to read as follows:

L. "Allowable expenses" means only actual out-of-pocket expenses incurred as the result of a repossession. The expenses must be reasonable and directly resulting from the repossessing, holding, preparing for disposition and disposing of the vehicle, and not otherwise reimbursed to the dealership. They are limited to the following charges (if allowable under applicable state law):

* * * * * * *

5. labor and associated parts and supplies furnished by the dealership for the repair, reconditioning or maintenance of the vehicle in preparation for disposition, computed at dealer cost (as defined in the Initial Compliance Report) with appropriate adjustments for any insurance or warranty recovery;

6. amounts paid to others for labor and associated parts and supplies purchased for the repair, reconditioning or maintenance of the vehicle in preparation for disposition;

7. cost of sales commissions paid for actual participation in the disposition of the particular vehicle, computed at a rate no higher than for the sale or lease, as applicable, of a similar, nonrepossessed vehicle in similar circumstances, but excluding portions of commissions attributable to the selling of service contracts, separately priced warranties, financing, or insurance;

* * * * * * *

10. expenses paid to others for communication (including telephone calls, postage, and military locator fees) and photocopying necessary in arranging for the repossession, holding, transportation, reconditioning, or disposition of the vehicle; and

11. amounts paid to insure the particular vehicle while holding it.

It is further ordered, That Paragraph IV.H.1 of the Order be modified to eliminate the following language:

1. submit to the Federal Trade Commission a summary report of the audit for that dealership, containing . . .

and substitute therefor the following:

1. prepare a summary report of the audit for that dealership, containing . . .

IN THE MATTER OF

GENERAL MOTORS CORPORATION, ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT

Docket 9074. Complaint Feb. 10, 1976—Decision, July 7, 1980*

This consent order requires, among other things, Chuck Olson Chevrolet, Inc. (Olson), an Oregon Motor vehicle dealer with its principal place of business located in Seattle, Wash., to adopt and adhere to "Repossession Accounting Procedures" maintained by General Motors Corporation; furnish all appropriate supervisory personnel with a copy of the procedures; and establish to the reasonable satisfaction of the Commission that it has paid all surpluses realized on repossessed vehicles returned by financing institutions other than General Motors Acceptance Corporation (GMAC) since February 10, 1973. (Surpluses generated from Olson vehicles which have been repossessed by GMAC must be paid by GMAC.)

Appearances

For the Commission: *Randall H. Brook, Ivan L. Orton* and *Dean A. Fournier.*

For the respondents: *Robert C. St. Louis, Aiken, St. Louis & Siljeg,* Seattle, Wash.

DECISION AND ORDER

The Commission having heretofore issued its complaint charging the respondents named in the caption hereof with violation of Section 5 of the Federal Trade Commission Act, as amended, and the respondents having been served with a copy of that complaint together with a proposed form of order; and

Respondent Chuck Olson Chevrolet, Inc., its attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by said respondent as to the Commission's jurisdiction, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in the complaint, and waivers and other provisions in accordance with the Commission's Rules; and

The Secretary of the Commission having thereafter, in accordance

* Complaint previously published at 95 F.T.C. 825.

with Section 3.25(c) of its Rules, withdrawn this matter from adjudication as to Chuck Olson Chevrolet, Inc.; and

The Commission having considered the matter and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 3.25(f) of its Rules, the Commission hereby makes the following jurisdictional findings and enters the following order:

1. Respondent Chuck Olson Chevrolet, Inc. is an Oregon corporation with its office and principal place of business located at 17545 Aurora Ave. North, Seattle, Washington.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding as to Chuck Olson Chevrolet, Inc., and of said respondent, and the proceeding is in the public interest.

ORDER

I.

It is ordered, That respondent Chuck Olson Chevrolet, Inc., a corporation, and its successors, assigns, officers, agents, representatives and employees, and any corporation, subsidiary, division or device through which they act directly or indirectly (including Viking Service Corporation doing business as Olson Triumph), shall forthwith (A) adopt and adhere to the "Repossession Accounting Procedures" maintained by General Motors Corporation pursuant to the disposition of Docket 9074 as to General Motors Corporation, and (B) deliver a copy of the Repossession Accounting Procedures to all appropriate supervisory personnel.

II.

It is further ordered, That respondent shall, no later than 60 days after service of this Order:

A. Establish to the reasonable satisfaction of the Commission that all surpluses (if any) generated from repossessed vehicles returned to respondent by financing institutions other than General Motors Acceptance Corporation between February 10, 1973 and the date of service of this Order have been paid.

B. File with the Commission a written report setting forth in detail the manner and form in which it has complied with this Order.

III.

It is further ordered, That respondent notify the Commission at least 30 days prior to any dissolution or other proposed change in the corporate respondent (such as assignment or sale resulting in the emergence of a successor corporation or corporations), or any other corporate change (including the creation or dissolution of subsidiaries) which may affect compliance obligations arising out of this Order.

IN THE MATTER OF

C. ITOH & CO. (AMERICA), INC.

MODIFYING ORDER IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION AND WOOL PRODUCTS LABELING ACTS

Docket C-2586. Decision, Oct. 22, 1974—Modifying Order, July 7, 1980

This order modifies a previous order to cease and desist issued October 22, 1974 against a New York City importer and distributor of fabrics (84 F.T.C. 1187, 40 FR 6482). The Commission has modified the order by limiting the bond provision to recycled wool products only. The order previously required posting of a bond on all wool products imported.

ORDER MODIFYING CEASE AND DESIST ORDER

In its request filed on April 30, 1980, the respondent petitioned the Commission, pursuant to Section 2.51 of its Rules of Practice, to reopen the proceedings and modify the order of October 22, 1974, entered in Docket C-2586. Respondent asks that the second *"It is further ordered"* paragraph be deleted from the order. The paragraph in question reads as follows:

It is further ordered, That respondent, C. Itoh & Co. (America), Inc., a corporation, its successors and assigns, and its officers, and respondent's representatives, agents, and employees, directly or through any corporation, subsidiary, division, or other device, do forthwith cease and desist from importing or participating in the importation of wool products into the United States except upon filing bond with the Secretary of the Treasury in a sum double the value of said wool products and any duty thereon, conditioned upon compliance with the provisions of the Wool Products Labeling Act of 1939.

In support of its request, the respondent has advanced a number of considerations intended to show changed conditions of fact since the order was issued and to show that the public interest will best be served by granting its request. It states that it has ensured that its imported wool products are correctly labeled by investigating the reputations of its overseas suppliers and purchasing only from those with an established record of exercising proper care and diligence in determining the fiber content of their merchandise and labeling it properly. As the result of its self-policing, it states that there have been no complaints with regard to the labeling of any of its importations of wool products in the five and one-half years that the order has been in effect. The respondent advised Commission staff, by letter dated May 5, 1980, that it is no longer importing the

reprocessed or reused wool products which gave rise to the complaint and is now importing wool and wool blend products.[1] It states further, that due to the high costs of the premiums charged by sureties on the bond, it can no longer hope to profitably continue to sell wool products. It cites as a competitive disadvantage the fact that many of its competitors are not subject to the bonding requirement and that bonds have not appeared in recent Commission orders under the Wool Products Labeling Act of 1939.

By letter dated May 28, 1980, the respondent advised staff that it will agree to a modification of the order to limit the bonding requirement to the wool products that gave rise to the complaint, recycled wool products. If the respondent resumes importing such products, the bond will be applicable. It will not, however, be required to continue to bear the financial burden of paying premiums to sureties on the wool and wool blend products that it is now importing.

Having considered the request, the Commission has concluded that the order should be modified to limit the bond provision to recycled wool products and that the modification will safeguard the public interest. Therefore,

It is ordered, That the second *It is further ordered* paragraph of the order, set forth above, be replaced by the following new paragraph:

It is further ordered, That respondent, C. Itoh & Co. (America), Inc., a corporation, its successors and assigns, and its officers, and respondent's representatives, agents, and employees, directly or through any corporation, subsidiary, division, or other device, do forthwith cease and desist from importing or participating in the importation of recycled wool products into the United States except upon filing bond with the Secretary of the Treasury in a sum double the value of said recycled wool products and any duty thereon, conditioned upon compliance with the provisions of the Wool Products Labeling Act of 1939.

It is further ordered, That the foregoing modification shall become effective upon service of this order.

[1] The Wool Products Labeling Act of 1939 has been amended to substitute the word "recycled" for the words "reprocessed" and "reused" (Pub. Law 96-242, 94 Stat. 344, May 5, 1980, eff. July 4, 1980).

336-345 O - 81 - 4

IN THE MATTER OF

NATIONAL TEA COMPANY, ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT AND SEC. 7 OF THE CLAYTON ACT

Docket 9126. Complaint, April 17, 1979—Decision, July 23, 1980

This consent order dismisses the complaint against Applebaums' Food Markets, Inc., and requires, among other things, a Rosemont, Ill. operator of a retail grocery store chain to divest itself, within six months from the effective date of the order, of all its right, title and interest in seven specified retail grocery stores in the Minneapolis-St. Paul area, to a Commission-approved acquirer. Further, for a ten-year period, the company (with certain minor exceptions) is prohibited from acquiring any retail grocery store business located in designated geographic areas without prior Commission approval.

Appearances

For the Commission: *Joseph Tasker, Jr., Richard K. Kudo* and *Chauncey Hopkins.*

For the respondents: *James T. Halverson, Sherman & Sterling,* New York City and *Victor S. Friedman, Fried, Frank, Harris, Shriver & Jacobson,* New York City.

COMPLAINT

The Federal Trade Commission, having reason to believe that the above-named respondents have entered into an agreement which, if consummated, would result in a violation of Section 7 of the Clayton Act, as amended, (15 U.S.C.18), and Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45), and that said agreement therefore constitutes a violation of Section 5(a)(1) of the Federal Trade Commission Act, as amended, (15 U.S.C.45 (a)(1)), and having found that a proceeding with respect to said violation is in the public interest, issues its complaint stating its charges as follows:

Definitions

1. For the purposes of this complaint, the following definitions shall apply:

(a) "retail food stores" are defined as retail establishments primarily engaged in selling food for home preparation and consumption;

(b) "retail grocery stores" are defined as retail food stores, including supermarkets, convenience stores, and delicatessens, selling: (1) a wide variety of canned or frozen foods, such as vegetables, fruits, and soups; (2) dry groceries, either packaged or in bulk, such as tea, coffee, cocoa, dried fruits, processed food and non-edible grocery items. In addition, these establishments often sell smoked and prepared meats, and fresh fish and poultry, fresh vegetables and fruits, and fresh or frozen meats.

(c) "National Tea Company" is defined herein to include National Tea Company and all of its wholly-owned and partially-owned subsidiaries.

NATIONAL TEA COMPANY

2. Respondent National Tea Company (National) is an Illinois corporation with its principal office at 9701 West Higgins Road, Rosemont, Illinois.

3. In 1978, National operated a chain of approximately 200 retail grocery stores located primarily in the central part of the United States, including the States of Alabama, North Dakota and Wisconsin.

4. National's total sales for the year ending December 31, 1977 were approximately $835,604,312. National ranks among the twenty largest retail grocery chains in the United States.

5. In 1978, National operated a chain of approximately 19 retail grocery stores in Metropolitan Minneapolis/St. Paul, Minnesota.

6. At all times relevant herein, National has engaged in commerce as "commerce" is defined in Section 1 of the Clayton Act, as amended, and Section 4 of the Federal Trade Commission Act, as amended.

APPLEBAUMS' FOOD MARKETS, INC.

7. Respondent Applebaums' Food Markets, Inc. (Applebaums') is a Minnesota corporation with its principal office at 222 East Plato Blvd., P. O. Box 43509, St. Paul, Minnesota.

8. In 1978, Applebaums' operated a chain of approximately 29 retail grocery stores located in the State of Minnesota.

9. Applebaums' total net sales for the year ending April 29, 1978 amounted to approximately $127,991,000. The total retail sales of its grocery stores for the year ending January 31, 1979 amounted to approximately $134,927,000.

10. In 1978 Applebaums' operated a chain of approximately 28

retail grocery stores in Metropolitan Minneapolis/St. Paul, Minnesota.

11. At all times relevant herein, Applebaums' has engaged in commerce as "commerce" is defined in Section 1 of the Clayton Act, as amended, and Section 4 of the Federal Trade Commission Act, as amended.

MERGER AGREEMENT

12. On or about January 29, 1979, National and Applebaums' entered into an "Agreement and Plan of Merger and Reorganization" under the terms of which a wholly-owned subsidiary of National will be merged into Applebaums' and National will purchase all of Applebaums' outstanding stock for cash. Applebaums' will, by the terms of this agreement, become a wholly-owned subsidiary of National. The practical result of this agreement, if consummated, would be the acquisition of Applebaums' by National.

TRADE AND COMMERCE RELEVANT LINE OF COMMERCE

13. A relevant line of commerce in which to assess National's proposed acquisition of Applebaums' is retail grocery store sales.

14. Concentration in the relevant line of commerce is high in the relevant section of the country alleged below.

RELEVANT SECTION OF THE COUNTRY

15. A relevant section of the country is Metropolitan Minneapolis/St. Paul, Minnesota (MPLS/St. Paul), which is defined herein to mean the five contiguous Minnesota counties of Anoka, Dakota, Hennepin, Ramsey and Washington.

16. In 1978, Applebaums' operated approximately 28 retail grocery stores in MPLS/St. Paul; it ranked as the third largest firm in the market, with a market share, based on currently available information, of approximately 10%.

17. In 1978, National operated approximately 19 retail grocery stores in MPLS/St. Paul; it ranked as the fifth largest firm in the market, with a market share, based on currently available information, of approximately 4 1/2%.

18. National and Applebaums' have been for many years and are now direct and substantial competitors of one another in the relevant line of commerce in MPLS/St. Paul.

19. National's proposed acquisition of Applebaums' would make

National the largest operator of retail grocery stores in MPLS/St. Paul.

EFFECTS OF THE MERGER

20. The effects of the proposed merger set forth in Paragraph 12 herein may be substantially to lessen competition or tend to create a monopoly in the relevant market, in violation of Section 7 of the Clayton Act, as amended, (15 U.S.C. 18), and the acquisition constitutes an unfair method of competition and an unfair act or practice within the meaning of Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45), in the following ways among others:

a) The elimination of actual competition between National and Applebaums' in MPLS/St. Paul;
b) increased concentration in the retail grocery store business in MPLS/St. Paul;
c) potentially weakening competition from independent retail grocery competitors of Applebaums' and National in the MPLS/St. Paul market by impairing the ability of their wholesale supplier to maintain existing levels of price and service; and
d) the encouragement of further acquisitions and mergers by and among other leading firms in the retail grocery store business.

VIOLATION CHARGED

21. The merger between National and Applebaums', if consummated, would for the reasons set forth herein constitute a violation of Section 7 of the Clayton Act, as amended, (15 U.S.C. 18), and Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45).

22. By entering into the agreement which would give rise to the violation described in Paragraph 24, herein, National and Applebaums' have violated Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45).

Decision and Order

The Commission having heretofore issued its complaint charging the respondents named in the caption hereof with violation of Section 5 of the Federal Trade Commission Act, as amended, and Section 7 of the Clayton Act, as amended, and the respondents

having been served with a copy of that complaint, together with a notice of contemplated relief; and

Respondent National Tea Company, its attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by National Tea Company of all the jurisdictional facts set forth in the complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by National Tea Company that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Secretary of the Commission having thereafter withdrawn this matter from adjudication in accordance with Section 3.25(c) of its Rules; and

The Commission having considered the matter and having thereupon accepted the executed consent agreement and having placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure described in Section 3.25(f) of its Rules, the Commission hereby makes the following jurisdictional findings and enters the following order:

1. Respondent National Tea Company is a corporation organized, existing and doing business under and by virtue of the laws of the State of Illinois, with its office and principal place of business located at 9701 West Higgins Road, in the City of Rosemont, State of Illinois.

2. Respondent Applebaums' Food Markets, Inc., was once a corporation organized, existing and doing business under and by virtue of the laws of the State of Minnesota, with its office and principal place of business located at 222 Plato Blvd., in the City of St. Paul, State of Minnesota. Applebaums' Food Markets, Inc., ceased to exist as a corporation when it was merged on July 27, 1979, into a wholly-owned subsidiary of National Tea Company.

3. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents, and the proceeding is in the public interest.

Order To Divest and Other Relief

I

As used in this order:

(A) "National" means National Tea Co., a corporation organized under the laws of Illinois with its principal executive offices at 9701

West Higgins Road, Rosemont, Illinois, and its directors, officers, agents and employees, and its subsidiaries, successors and assigns.

(B) "Applebaums" means Applebaums' Food Markets, Inc., a corporation once organized under the laws of Minnesota with its principal executive offices at 222 Plato Blvd., St. Paul, Minnesota, and which was merged on July 27, 1979 into a wholly-owned subsidiary of National, at which time Applebaums as a corporation ceased to exist.

(C) "Retail grocery stores" are retail food stores classified under Bureau of Census Industry Classification No. 541, including supermarkets, convenience stores and delicatessens, which primarily sell a wide variety of canned or frozen foods, such as vegetables, fruits and soups; dry groceries, either packaged or in bulk, such as tea, coffee, cocoa, dried fruits, processed food, and non-edible grocery items. In addition, these stores often sell smoked and prepared meats, and fresh fish and poultry, fresh vegetables and fruits, and fresh or frozen meats.

(D) "The Minneapolis-St. Paul Area" means the area encompassed by the Minnesota counties of Anoka, Dakota, Hennepin, Ramsey and Washington.

(E) "Applebaums stores" means those retail grocery stores in the Minneapolis/St. Paul area formerly owned by Applebaums, all of which were acquired by National on July 27, 1979.

(F) "National stores" means those retail grocery stores in the Minneapolis/St. Paul area owned by or operated by National on or after the date on which this Order becomes final, including the Applebaums stores.

(G) The "disposition stores" means the following National ("N") stores and Applebaums ("A") stores:

1. N-80 (2326 Louisiana, St. Louis Park)
2. N-91 (3115 E. 38th St., Minneapolis)
3. N-99 (150 Apache Plaza, St. Anthony Village)
4. N-210 (4300 Xycon Ave., New Hope)
5. N-803 (8948 University Ave., St. Paul)
6. N-130 (1901 W. 80th St., Bloomington)
7. A-8 (900 E. Maryland, St. Paul)

(H) "May Brothers" means May Brothers Company, a wholesale supplier of groceries and related products with its principal office located at 3501 Marshall St., Northeast, Minneapolis, Minnesota.

(I) "Acquisition," "acquire," "merger," or "merge with" includes all other forms of arrangement by which National may obtain all or

any part of the market share of any other retail grocery store or stores.

II

It is ordered, That within six months from the date on which this Order becomes final, National shall divest itself of all of its right, title and interest in the disposition stores. During this period, National shall continue to operate said properties as retail grocery stores. Divestiture shall be made only to an acquiror or acquirors approved in advance by the Federal Trade Commission. The purpose of the divestiture required by this paragraph is to assure the continued operation of the disposition stores as retail grocery stores and their survival as viable competitors in the Minneapolis-St. Paul area.

III

It is further ordered, That at the request of May Brothers National shall do the following:

(A) For a period of one year from the date on which this Order becomes final, National shall continue to purchase from May Brothers, when averaged over the one-year period, at least fifty percent of the dry grocery products purchased by National for the Applebaums stores;

(B) For a period of five years from the date on which this order becomes final, National shall make annual purchases of no less than six million dollars ($6,000,000.00) of dry groceries from May Brothers for the National stores, and, for a period of five years from the date on which this order becomes final, National shall maintain May Brothers as the first alternative source for the dry grocery products requirements of the National stores; and

(C) For a period of five years from the date on which this order becomes final May Brothers shall be the exclusive frozen food supplier of the National stores;

provided, however, that this paragraph shall have effect only so long as May Brothers continues to offer National competitive quality and prices for such purchases.

IV

It is further ordered, That for a period of ten (10) years from the date on which this order becomes final, National shall not merge

with or acquire, or merge with or acquire and thereafter hold, directly or indirectly through subsidiaries or in any other manner, without the prior approval of the Federal Trade Commission, the whole or any part of the stock or assets of any individual, firm, partnership, corporation or other legal or business entity which directly or indirectly owns or operates any retail grocery store, where such acquisition or merger involves five or more such retail grocery stores, any one of which is located in any of the following areas:

(A) In Minnesota, Wisconsin, Indiana, Missouri, Illinois, Louisiana or Mississippi; or

(B) Within five hundred (500) miles of any warehouse owned or operated by National at the time of such acquisition or merger and which is engaged in the shipment of products to retail grocery stores; or

(C) Within three hundred (300) miles of any retail grocery store owned or operated by National at the time of such acquisition or merger.

V

It is further ordered, That, in the event National withdraws from the business of operating retail grocery stores in the Minneapolis/St. Paul area prior to the expiration of paragraph IV of this order, National shall divest all of its right, title and interest in the National stores to an acquiror or acquirors approved in advance by the Federal Trade Commission. The purpose of this paragraph is to assure that National's withdrawal from the Minneapolis/St. Paul area is accomplished in a manner which, in the opinion of the Federal Trade Commission, will best promote, preserve, and protect competition among retail grocery stores in that area.

VI

It is further ordered, That within sixty (60) days from the date on which this order becomes final and every sixty (60) days thereafter until the divestiture required by paragraph II of this order is completed, National shall submit to the Federal Trade Commission a written report setting forth in detail the manner and form in which National intends to comply, is complying, and has complied with the terms of this order and such additional information relating thereto as may from time to time be required. In addition, upon written request of the staff of the Federal Trade Commission, National shall

submit such reports in writing with respect to the other requirements of this order as may from time to time be requested.

VII

It is further ordered, That National notify the Federal Trade Commission at least thirty (30) days prior to any proposed corporate changes, such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporation, which may affect compliance with the obligations arising out of this order.

VIII

It is further ordered, That the complaint against Applebaums' Food Markets, Inc., be, and it hereby is, dismissed.

IN THE MATTER OF

CLINIQUE LABORATORIES, INC.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-3027. Complaint, July 23, 1980—Decision, July 23, 1980

This consent order requires, among other things, a New York City manufacturer and distributor of cosmetics and related products to cease establishing, fixing or maintaining resale prices for its products and compelling adherence to suggested prices through coercion or otherwise. The firm is prohibited from seeking the identity of dealers who fail to conform to established prices and taking adverse action against them. The order further bars the company from restricting the lawful use of brand names and trademarks in the advertising and sale of its products, and withholding earned cooperative advertising credits or allowances from recalcitrant dealers. Additionally, respondent is prohibited from suggesting retail prices for its products for a specified period.

Appearances

For the Commission: *Jeffrey Klurfeld* and *Karen Chandler.*

For the respondent: *Joshua F. Greenburg* and *Louis A. Shapiro,* New York City, and *Saul H. Magram,* House Counsel, New York City.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that Clinique Laboratories, Inc., a corporation, hereinafter sometimes referred to as respondent, has violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges as follows:

For purposes of this complaint, the following definitions shall apply:

A. "Product"

"Product" is defined as any item of cosmetic, fragrance or soap, any accessory containing any item of cosmetic, fragrance or soap, or any related accessory, including but not limited to, any applicator or brush, which is manufactured, offered for sale or sold by respondent.

In addition to the foregoing, "product" is defined to include any item which is manufactured, offered for sale or sold by respondent for resale to consumers together with any "product" as defined hereinabove.

B. "Dealer"

"Dealer" is defined as any person, partnership, corporation or firm which sells any product in the course of its business.

C. "Resale Price"

"Resale Price" is defined as any price, price floor, price ceiling, price range, or any mark-up, formula or margin of profit used by any dealer for pricing any product. Such term includes, but is not limited to, any suggested, established or customary resale price as well as the retail price in effect at any dealer.

PARAGRAPH 1. Respondent Clinique Laboratories, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York with its office and principal place of business located at 767 Fifth Ave., New York, New York.

PAR. 2. Respondent is now, and for some time last past, has been engaged in the manufacture, advertising, offering for sale, sale and distribution of cosmetics, fragrances, soaps and related accessories.

PAR. 3. Respondent maintains, and has maintained, a substantial course of business, including the acts and practices as hereinafter set forth, which are in or affect commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended.

PAR. 4. Respondent sells and distributes its products directly to retail dealers located throughout the United States who resell respondent's products to the general public.

PAR. 5. In the course and conduct of its business, and at all times mentioned herein, respondent has been, and now is, in substantial competition in or affecting commerce with corporations, firms and individuals engaged in the manufacture, advertising, offering for sale, sale or distribution of merchandise of the same general kind and nature as merchandise manufactured, advertised, offered for sale, sold or distributed by respondent.

PAR. 6. In the course and conduct of its business as above described, respondent has for some time last past effectuated and pursued a policy throughout the United States to fix, control, establish, manipulate and maintain the resale prices at which certain of its dealers advertise, offer for sale and sell its products.

PAR. 7. By various means and methods, respondent has effectuated

and enforced the aforesaid practice and policy by which it can and does fix, control, establish, manipulate and maintain the resale prices at which its products are advertised, offered for sale and sold by certain of its dealers.

PAR. 8. By means of the aforesaid acts and practices and more, respondent, in combination, agreement, understanding and conspiracy with certain of its dealers and with the acquiescence of certain other dealers, has established, maintained and pursued a planned course of action to fix and maintain certain specified uniform prices at which products will be resold.

PAR. 9. The aforesaid acts and practices of respondent have been and are now having the effect of hampering and restraining competition in the resale and distribution of respondent's products, and, thus, are to the prejudice and injury of the public, and constitute unfair methods of competition in or affecting commerce or unfair acts and practices in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act. The acts and practices of respondent as herein alleged, are continuing and will continue in the absence of the relief herein requested.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the San Francisco Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act; and

The respondent, its attorneys, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the

procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent Clinique Laboratories, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York, with its office and principal place of business located at 767 Fifth Ave., in the City of New York, State of New York.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

ORDER

For the purposes of this Order, the following definitions shall apply:

A. "Product"

"Product" is defined as any item of cosmetic, fragrance or soap, any accessory containing any item of cosmetic, fragrance or soap, or any related accessory, including but not limited to any applicator or brush, which is manufactured, offered for sale or sold by respondent.

In addition to the foregoing, "product" is defined to include any item which is manufactured, offered for sale or sold by respondent for resale to consumers together with any "product" as defined hereinabove.

B. "Dealer"

"Dealer" is defined as any person, partnership, corporation or firm which sells any product in the course of its business.

C. "Resale Price"

"Resale Price" is defined as any price, price floor, price ceiling, price range, or any mark-up, formula or margin of profit used by any dealer for pricing any product. Such term includes, but is not limited to, any suggested, established or customary resale price as well as the retail price in effect at any dealer.

It is ordered, That respondent Clinique Laboratories, Inc., a corporation, its successors and assigns, and respondent's officers, agents, representatives and employees, directly or indirectly, or through any corporation, subsidiary, division or other device, in connection with the manufacture, advertising, offering for sale, sale or distribution of any product in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from:

I.

1. Fixing, establishing, controlling or maintaining, directly or indirectly, the resale price at which any dealer may advertise, promote, offer for sale or sell any product.

2. Requesting, requiring or coercing, directly or indirectly, any dealer to maintain, adopt or adhere to any resale price.

3. Requesting or requiring, directly or indirectly, any dealer to report the identity of any other dealer who deviates from any resale price; or acting on any reports or information so obtained by threatening, intimidating, coercing or terminating said dealer.

4. Requesting or requiring that any dealer refrain from or discontinue selling or advertising any product at any resale price.

5. Hindering or precluding the lawful use by any dealer of any brand name, trade name or trademark of respondent in connection with the sale or advertising of any product at any resale price.

6. Conducting any surveillance program to determine whether any dealer is advertising, offering for sale or selling any product at any resale price, where such surveillance program is conducted to fix, maintain, control or enforce the resale price at which any product is sold or advertised.

7. Terminating or taking any other action to restrict, prevent or limit the sale of any product by any dealer because of the resale price at which said dealer has sold or advertised, is selling or advertising, or is suspected of selling or advertising any product.

8. Threatening to withhold or withholding earned cooperative advertising credits or allowances from any dealer, or limiting or restricting the right of any dealer to participate in any cooperative advertising program for which it would otherwise qualify, because of the resale price at which said dealer advertises or sells any product, or proposes to sell or advertise any product.

9. Making any payment or granting any other consideration or benefit to any dealer because of the resale price at which any other dealer has sold or advertised any product.

II.

1. For a period of three (3) years from June 30, 1980, orally suggesting or recommending any resale price to any dealer.

2. For a period of three (3) years from June 30, 1980, communicating in writing any resale price to any dealer.

3. After said three (3) year period, respondent shall not suggest or recommend to any dealer any resale price on any list or order form, or in any catalogue or stock control book, unless it is clearly

and conspicuously stated on each page thereof where any suggested or recommended resale price appears, the following:

THE RETAIL PRICES QUOTED HEREIN ARE SUGGESTED ONLY. YOU ARE COMPLETELY FREE TO DETERMINE YOUR OWN RETAIL PRICES.

III.

1. Nothing contained in this Order shall preclude respondent from publishing or printing any resale price which is specified by any dealer for use or inclusion in any advertising, mailer or promotional material which said dealer intends to disseminate to consumers; *provided, however,* that for a period of three (3) years from June 30, 1980, in connection with each advertising, mailer or promotional material which any dealer intends to disseminate to consumers, respondent shall make a written request to said dealer to specify its resale price(s), and shall disclose therein in a clear and conspicuous manner the following:

CLINIQUE DEALERS ARE COMPLETELY FREE TO SPECIFY RETAIL PRICES OF THEIR OWN CHOOSING FOR INCLUSION IN THIS [ADVERTISING, MAILER OR PROMOTIONAL MATERIAL]. PLEASE INSERT THOSE RETAIL PRICES YOU WISH TO BE PRINTED ON THIS [ADVERTISING, MAILER OR PROMOTIONAL MATERIAL].

2. After said three (3) year period, respondent shall not suggest any resale price to any dealer for use or inclusion in any advertising, mailer or promotional material which said dealer intends to disseminate to consumers, unless respondent, in connection with each advertising, mailer or promotional material, makes a written request to said dealer to review said advertising, mailer or promotional material for its resale price(s), and discloses therein in a clear and conspicuous manner the following:

CLINIQUE DEALERS ARE COMPLETELY FREE TO SPECIFY RETAIL PRICES OF THEIR OWN CHOOSING FOR INCLUSION IN THIS [ADVERTISING, MAILER OR PROMOTIONAL MATERIAL]. YOU MAY CHANGE THE PRICES WE HAVE SUGGESTED.

IV.

It is further ordered, That respondent shall:

1. Within sixty (60) days after service of this Order, mail under separate cover a copy of the enclosure set forth in the attached Exhibit A to each of its present accounts. An affidavit shall be sworn to by an official of respondent verifying that the attached Exhibit A was so mailed.

2. Mail under separate cover a copy of the enclosure set forth in the attached Exhibit A to any person, partnership, corporation or

firm that becomes a new account within three (3) years after service of this Order.

3. For a period of three (3) years from the date of service of this Order, mail semiannually under separate cover a copy of the enclosure set forth in the attached Exhibit B to each of respondent's then present accounts.

V.

It is further ordered, That respondent shall forthwith distribute a copy of this Order to all operating divisions of said corporation; and, for a period of five years from the date of service of the Order, to all personnel, agents or representatives having sales, advertising or policy responsibilities with respect to the subject matter of this Order, and that respondent secure from each such person a signed statement acknowledging receipt of said Order.

VI.

It is further ordered, That respondent notify the Commission at least thirty (30) days prior to any proposed change in the respondent such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the respective corporation which may affect compliance obligations arising out of the Order.

VII.

It is further ordered, That respondent shall within seventy-five (75) days after service upon it of this Order, file with the Commission a report, in writing, setting forth in detail the manner and form in which it has complied with this Order.

EXHIBIT A

Dear Retailer:

This letter is being sent to all Clinique accounts. On [date], Clinique Laboratories, Inc. agreed to the entry of a Consent Order with the Federal Trade Commission concerning certain distribution practices. This Consent Order was entered into for settlement purposes only and does not constitute an admission that Clinique violated the law. As part of that Consent Order, we are obligated to send you this letter.

Clinique wants its accounts to know and understand the following:

1. You can advertise and sell Clinique products at any price you choose.

2. Clinique will not take any action against you, including termination, because of the price at which you advertise or sell Clinique products.

3. Clinique will not suggest retail prices for any product until July 1, 1983.

4. The price at which you sell or advertise Clinique products will not affect your right to lawfully use Clinique trademarks or other identification in your sale or advertising of products bearing Clinique trademarks or identification.

5. You are free to participate in any cooperative advertising program sponsored by Clinique for which you would otherwise qualify, and to receive any advertising credit or allowance allowed thereunder regardless of the price at which you advertise a Clinique product.

6. Clinique will continue to publish or print mailers, advertising and other promotional materials which you intend to disseminate to consumers containing retail prices which you specify. Until July 1, 1983, in connection with each advertising, mailer or promotional material we will publish for you to disseminate to consumers, we will be requesting in writing that you specify the retail prices you wish to be printed on these materials.

After July 1, 1983, we will send you materials for your review which may contain our suggested retail prices. You are completely free, however, to change these prices, and we will then print the materials with the retail prices which you have specified.

7. The price at which a store sells or advertises a Clinique product is its own business. Clinique does not want to be informed by an account of the price at which any other store sells or advertises any Clinique product.

If you have any questions regarding the Consent Order or this letter, please call _____.

_____

for Clinique Laboratories, Inc.

EXHIBIT B

Dear Retailer:

We wish to remind you of the following:

1. You can advertise and sell Clinique products at any price you choose.

2. Clinique will not take any action against you, including termination, because of the price at which you advertise or sell Clinique products.

3. Clinique will not suggest retail prices for any product until July 1, 1983.

4. The price at which you sell or advertise Clinique products will not affect your right to lawfully use Clinique trademarks or other identification in your sale or advertising of products bearing Clinique trademarks or identification.

5. You are free to participate in any cooperative advertising program sponsored by Clinique for which you would otherwise qualify, and to receive any advertising credit or allowance allowed thereunder regardless of the price at which you advertise a Clinique product.

6. Clinique will continue to publish or print mailers, advertising and other promotional materials which you intend to disseminate to consumers containing retail prices which you specify. Until July 1, 1983, in connection with each advertising, mailer or promotional material we will publish for you to disseminate to

consumers, we will be requesting in writing that you specify the retail prices you wish to be printed on these materials.

After July 1, 1983, we will send you materials for your review which may contain our suggested retail prices. You are completely free, however, to change these prices, and we will then print the materials with the retail prices which you have specified.

7. The price at which a store sells or advertises a Clinique product is its own business. Clinique does not want to be informed by an account of the price at which any other store sells or advertises any Clinique product.

If you have any questions, please call _____.

_____

for Clinique Laboratories, Inc.

IN THE MATTER OF

FRED MEYER, INC.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-3028. Complaint, July 23, 1980—Decision, July 23, 1980

This consent order requires, among other things, a Portland, Ore. operator of a chain of retail stores to provide each charge account customer having an outstanding credit balance with a periodic statement setting forth the amount of the credit balance; and enclose with regular monthly statements, a notice advising that credit balances are refundable upon request. Refunds of credit balances must be made upon request or automatically at the end of a six-month period. The firm is further required to refund, with interest, all unpaid credit balances existing between January 1, 1974 and the effective date of the order. The order additionally requires that the firm notify layaway customers who had not completed their purchases during the fourteen (14) months prior to entry of the order that they have the option of either completing the transaction or receiving a refund of the layaway account credit balance; refund credit balances to any customer who indicates, in response to a notice, that the purchase was not completed and the customer received no reimbursement or credit on other merchandise; and maintain specified records for at least three years.

Appearances

For the Commission: *Dennis D. McFeely, Ivan L. Orton,* and *James M. Cox.*

For the respondent: *Robert Ridgley, Davies, Biggs, Strayer, Stoel & Bollie,* Portland, Oreg.

COMPLAINT

The Federal Trade Commission, having reason to believe that Fred Meyer, Inc., a corporation, has violated the provisions of the Federal Trade Commission Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint as follows:

PARAGRAPH 1. Respondent Fred Meyer, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Oregon, with its principal office and place of business located at 3800 S.E. 22nd, Portland, Oregon.

All allegations herein made in the present tense include the past tense.

PAR. 2. Respondent Fred Meyer, Inc. operates a chain of retail

stores selling food, drug, variety goods and other general merchandise in Oregon, Montana and Washington. It also operates a wholesale grocery business in Spokane, Washington. The volume of its wholesale and retail business is substantial.

PAR. 3. In the course and conduct of its business as aforesaid, respondent causes, directly and indirectly, merchandise to be shipped and distributed from manufacturing and processing plants or from other sources of supply to its warehouses and distribution centers or retail stores located in states other than the state of origination, distribution or storage of said merchandise. Purchasers of some merchandise sold by respondent reside outside the state where the merchandise is purchased and soon after such purchase, transport the merchandise across state lines to their place of residence. By these and other acts and practices, respondent maintains a substantial course of business in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act.

PAR. 4. In the ordinary course and conduct of its business described above, respondent permits certain of its customers who qualify for credit to charge purchases to revolving credit accounts. These customers are individuals, municipalities, charities, and businesses. On occasion, customers' charge account balances consist of credits to the customers' account which represent an amount of money owed to the customer by the respondent. These credit balances are the result of, among other things, overpayments by the customer or credits for the purchase price of returned merchandise.

PAR. 5. Typical and illustrative of respondent's practices in handling the credit balances of its customers are the following:

1. Respondent regularly fails to send out any statement or notification to its customers of the existence of a credit balance in the customers' account.

2. Respondent fails to inform charge customers that they have a continuing right to request and receive a refund in the amount of their credit balances.

3. Respondent transfers credit balances out of charge customers' accounts without notice to the charge customers.

4. Except upon request, respondent does not refund credit balances to charge customers.

Through such acts and practices, respondent has retained in its possession substantial dollar amounts of credit balances belonging to its customers and has consequently deprived customers of substantial sums of money belonging to those customers. Therefore, the acts and practices described in this paragraph are unfair and deceptive.

PAR. 6. In the ordinary course and conduct of its business described above, respondent permits its customers to make purchases under a layaway plan. Under the plan a customer makes a downpayment which reserves the merchandise. The customer makes payments on the layaway account until the merchandise is paid for. The merchandise is then given to the customer. On occasion, customer's layaway account balances consist of credits to the customers' account which represent an amount of money owed to the customer by the respondent. These credit balances are the result of, among other things, cancellation of the layaway by the customer or respondent, resulting in a credit to the layaway account.

PAR. 7. Typical and illustrative of respondent's practices in handling the credit balances of its layaway customers are the following:

1. Respondent fails to inform layaway customers that they have a continuing right to request and receive a refund in the amount of their credit balances.
2. Respondent transfers credit balances out of layaway customers' accounts without notice to the customers.
3. Except upon request, respondent does not refund credit balances to layaway customers.

Through such acts and practices, respondent has retained in its possession substantial dollar amounts of layaway credit balances belonging to its customers and has consequently deprived customers of substantial sums of money belonging to those customers. Therefore, the acts and practices described in this paragraph are unfair and deceptive.

PAR. 8. The acts and practices of respondent as set forth in Paragraphs Four, Five, Six and Seven above, were and are to the prejudice and injury of the public and constitute unfair and deceptive acts and practices in or affecting commerce in violation of Section 5(a)(1) of the Federal Trade Commission Act.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the Seattle Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act; and

The respondent, its attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent Fred Meyer, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Oregon, with its office and principal place of business located at 3800 S.E. 22nd, in the City of Portland, State of Oregon.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

ORDER

I.

Charge Account Credit Balances

It is ordered, That respondent Fred Meyer, Inc., a corporation, its successors and assigns, and its representatives, officers, agents, and employees, directly or through any corporation, subsidiary, division or other device, except for Fred Meyer Savings & Loan Association and the wholesale division of Round-Up Company, in connection with the management of credit balances arising subsequent to the service of this Order, on charge accounts created or maintained incident to the sale of merchandise or services to credit customers for use or consumption, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, shall:

A. Mail or deliver to each credit customer before the end of the next billing cycle, for each credit customer's billing cycle at the end

of which there is an outstanding credit balance in excess of one dollar ($1.00):

1. a periodic statement which clearly sets forth the amount of the credit balance, and

2. include the following disclosure clearly and conspicuously in twelve-point or larger type, entirely on the front side of, or enclosed with, the periodic statement reflecting a credit balance, separated from any other written matter, and accompanied by a pre-addressed return envelope:

WE OWE YOU MONEY

The enclosed statement shows a "credit balance." This is money we may owe you. If you want a refund now, please mail this statement back to us in the enclosed envelope. Write on it that you want a refund.

If you don't ask for a refund and if you don't buy anything more from us through your account, we will send you your refund automatically within 6 months if it's over $1 (and is still due you).

If your credit balance is $1 or less, we won't send it to you if you don't ask for it. But even if we don't hear from you, we will credit it against your next purchase.

B. If a purchase is made on an account in which there is a credit balance, apply the amount of that balance to such purchase.

C. Refund the full amount of each credit balance within thirty (30) days after receiving a credit customer's written request except to the extent that such amount has already been credited against further purchases on the account.

D. Refund the full amount of each credit balance in excess of one dollar ($1.00) within thirty (30) days after the end of the sixth consecutive monthly billing cycle at the end of each of which a credit balance has existed. The amount to be refunded shall be the credit balance existing at the end of the sixth month.

E. Refrain from writing off, deleting or transferring any credit balance in excess of $1.00 until a refund has been made or until the credit customer has made a fully offsetting purchase unless respondent has taken all actions required by Paragraph III of this Order with respect to that account.

F. If respondent believes a credit balance to be not owed it need not:

1. apply the amount of the credit balance to the purchase pursuant to I.B if respondent sends to the credit customer an individualized written explanation and supporting documentation in support of its belief. This documentation shall be provided in the

manner described in III.B and shall be mailed within 30 days of the purchase. Respondent may, if it otherwise complies with this paragraph, send corrected billings to credit customers which respondent subsequently believes were sent erroneous billings.

2. refund pursuant to I.C and I.D if respondent sends to the credit customer an individualized written explanation and supporting documentation. This documentation shall be provided in the manner described in III.B and within the time that Paragraphs I.C and I.D require that refunds be made.

G. Paragraph F does not permit respondent to collect or attempt to collect (including charging to a customer's account) any amounts paid to a customer which respondent subsequently believes were paid in error.

II.

Definition

"Credit customer" as used in Section II only shall exclude all firms from which respondent purchased merchandise or services since January 1, 1974.

It is further ordered, That respondent shall:

A. Refund to each credit customer the amount of each credit balance in the amount of more than one dollar ($1.00):

1. which was created or existed at any time between January 1, 1974 and the date of service of this Order,
2. and which has not been fully refunded to a credit customer prior to the date of the service of this Order,
3. unless such credit balance is not owed to the credit customer as determined by the procedures provided in Paragraph II.D, or
4. unless the credit customer makes or has made a fully offsetting purchase on the account between January 1, 1974 and the time provided in Paragraph VII.C for the filing of a compliance report.

B. Pay to each credit customer to whom a credit balance is refunded, interest on the amount of the credit balance computed at the rate of .5 percent per month from the date the credit balance was transferred out of each credit customer's account.

C. Effect complete compliance with the provisions of Paragraphs

II.A and B of this Order within one hundred eighty (180) days after the date of service of this Order.

D. For the purposes of II.A.3 of this Order, whether a credit balance is not owed to a credit customer shall be determined by a firm of Certified Public Accountants acceptable to the Regional Director of the Seattle Regional office of the Commission. Respondent shall retain such firm to examine such originals or copies of records and papers which respondent believes justify a determination that any credit balance covered by this Order is not in fact owed to a credit customer. If the CPA firm agrees with respondent, respondent is not required to refund the credit balance. As an alternative to requesting a determination from a CPA firm, the respondent may pay the credit balance.

All credit balances other than those which the CPA firm agrees are not owed shall be considered, for the purposes of this Order, to be owed to the credit customer and shall be refunded pursuant to Paragraph II.A. The CPA firm shall be directed by respondent to make a written report of each finding in agreement with respondent through use of the certifying form attached as Exhibit A. Such report shall be included as part of the compliance report required by Paragraph VII.

III.

It is further ordered, That:

A. Each refund required by this Order shall be given to the credit customer by mailing a check payable to the order of the customer.

B. Each check sent pursuant to Paragraphs I.C, I.D, II.A, II.B, IV.C, and V.B and each disclosure and letter sent pursuant to Paragraphs I.A and V.A of this Order, shall be mailed First Class in an envelope which clearly states respondent's name and address in the upper lefthand corner, to the customer's most recent address shown in respondent's records, with the notation "Address Correction Requested" on the envelope. In the event that any such check, disclosure or letter concerning a credit balance or payment in the amount of ten dollars ($10.00) or more is returned to respondent undelivered, respondent shall seek to obtain the most current address available for the customer by consulting, in the following order, (1) telephone directories and city directories, and (2) a consumer reporting agency. If a new address is obtained, respondent shall then remail such check, disclosure, or letter First Class to the customer at the most current address obtained.

C. For each credit balance unpaid despite performance of the steps set out in Paragraphs III.A and III.B, respondent:

1. shall maintain the full amount of the credit balance in the customer's account for one year from the date on which the most recent mailing was returned; and
2. need not send any additional disclosure or refund with respect to that credit balance except as provided in Paragraph III.D of this Order.

D. Respondent shall, within thirty (30) days of any credit customer's written request for a refund of a credit balance which had been reflected at any time on the customer's account, either refund the amount requested or send the customer an individualized written explanation, with supporting documentation, when available, of the reason(s) for refusing to refund the amount requested.

IV.

Layaway Account Balances

For the purpose of this Order, the term "layaway" shall mean any transaction whereby the customer agrees to purchase merchandise at the time of the transaction, by means of a downpayment and subsequent payment or payments, with the respondent retaining possession of the merchandise until the agreed payment or payments are completed.

It is ordered, That respondent Fred Meyer, Inc., a corporation, its successors and assigns, and its representatives, officers, agents, and employees, directly or through any corporation, subsidiary, division or other device, except for Fred Meyer Savings & Loan Association and the wholesale division of Round-Up Company, in connection with the management of layaway balances arising subsequent to the service of this Order, on layaway accounts created or maintained incident to the sale of merchandise to layaway customers, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, shall:

A. Mail to each layaway customer:

1. within twenty (20) days after the end of the period designated in the layaway agreement to make full payment for the merchandise,
2. if the payments received by respondent have not been returned to the customer, and

3. if the merchandise has not been delivered to the customer, and

4. before the merchandise is returned to stock and before making any entries in the layaway account which would close out the account,

the following disclosure clearly and conspicuously in twelve-point or larger type, entirely on one side of a single piece of paper, separated from any other written matter:

WE OWE YOU MONEY

(Date of mailing to be inserted here)

You haven't fully paid for your recent layaway purchase at our (name of store) store. You can fully pay for your purchase within 10 days from the above date. Or you can get a refund from us for the amount you have paid (less 35 cents handling charge). If you want a refund, come to the department of the store where you have the layaway not later than (insert date 10 days from notice) and ask for your money. You also have the choice of getting a credit to purchase other merchandise. Please bring this notice with you. If you don't ask for a refund or a credit, we will send you a check automatically within 45 days if the amount we owe you is more than $1.00.

Respondent may insert in the above notice a different handling charge that is reasonable in comparison with a 35 cent charge.

B. Defer returning layaway merchandise to stock until 11 days after the mailing of the notice specified in IV.A. and allow completion of the layaway purchase within 10 days after the mailing of the notice.

C. Refund the full amount paid by the layaway customer (less 35 cents or other charge that is reasonable in comparison with a 35 cent charge) if the amount is in excess of one dollar ($1.00) within 45 days of the date of the notice specified in Paragraph IV.A unless the layaway customer has completed the purchase of the layaway merchandise. Such refund shall be made by sending a check in the amount of the layaway balance to each customer owed a refund. Respondent shall thereafter follow the provisions of Paragraph III.B (pertaining otherwise to credit balances) with respect to such checks. A credit issued by respondent at its store for the purchase of other merchandise in lieu of a cash refund, solely at the option of the layaway customer, shall be considered a refund for purposes of this Section IV.

D. Refrain from writing off, deleting, or transferring any layaway account balance until a refund has been made, or until 30 days after the procedures of Paragraphs III.A and III.B are fully complied

with, or until the customer has completed the purchase of the layaway merchandise.

V.

It is further ordered, That respondent:

A. Identify all layaway account customers which are included in all the layaway account master listings printed out during the 14 months prior to the entry of this order as having layaway balances in excess of $1.00. Mail to each customer so identified a letter identical to Attachment B in form, spacing, and layout, without the inclusion of any other written material. In sending out Attachment B, respondent shall fill in at the end of question 1 the month or months and year that the layaway account first appeared on its records. Respondent shall thereafter follow the provisions of Paragraph III.B (pertaining otherwise to credit balances) with respect to each such letter.

B. Make payment in full by sending a check in the amount of the layaway balance to each customer identified by the procedure in Paragraph V.A who has responded negatively to questions 5(a) and 5(b) on Attachment B, unless question 1 is answered negatively or 4 is answered affirmatively. Respondent shall thereafter follow the provisions of Paragraph III.B (pertaining otherwise to credit balances) with respect to each such check.

VI.

It is further ordered, That respondent shall maintain complete business records relative to the manner and form of its continuing compliance with this Order, including but not limited to the name and address of each credit and layaway customer who requested a refund of a credit or layaway balance but whose request was refused, the date and amount of the request, and the date and reason(s) for the refusal. Respondent shall retain all such records and data for at least three years and shall, upon reasonable notice, make them available for examination and copying by representatives of the Federal Trade Commission. Upon the request of a representative of the Federal Trade Commission, respondent shall compile a list of the credit and layaway balances refunded, to include the account number and dollar amount of each such account.

VII.

It is further ordered, That respondent shall:

A. Forthwith distribute a copy of this Order to each of its present and future personnel having policy responsibilities with respect to the subject matter of this Order, including but not limited to the Vice-President for Finance, Controller, Accounting Operations Manager, Accounts Payable Supervisor, Accounts Receivable Supervisory Clerk, and the assistants to the above.

B. Notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondent such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporation which may affect compliance obligations arising out of the order.

C. File with the Commission a written report, within sixty (60) days after service of this Order, setting forth in detail the manner and form in which it has complied with this Order to that time, *provided, however,* respondent shall file with the Commission within 180 days after service of this Order, a written report setting forth the following data:

1. The number of accounts and total dollar amounts of credit balances identified pursuant to Paragraph II.A of this Order and:

a. refunded by respondent;

b. determined to be not owed pursuant to the procedures of Paragraph II.D;

c. offset by further purchases made on the customer's account; or

d. retained by respondent because the customer could not be located pursuant to the procedures of Paragraph III.B.

2. The number of accounts and total dollar amounts of layaway balances identified pursuant to Paragraph V.A of this Order and

a. refunded by respondent;

b. determined to be not owed because the layaway merchandise was received;

c. determined to be not owed because a credit was issued for the purchase of other merchandise;

d. determined to be not owed because a refund had already been received.

ATTACHMENT A

This certifies that I have reviewed the following accounts and find them to be excluded from the Consent Decree pursuant to Paragraph II.D for the reason indicated:

ACCOUNT NUMBER	BALANCE	REASON

Dated this _____ day of _____, 19____.

_____

ATTACHMENT B

Dear Customer:

We may owe you some money. Our records show that you may have started making payments on a layaway numbered _____.

Please answer the questions below. Return the bottom part of this page in the enclosed envelope. We will then check our records. If we owe you money we will mail it to you. We will not try to collect any money from you.

Sincerely yours,

Fred Meyer, Inc.

.....

Your Name _____
(Print)

_____
(Address)

1. Did you start a layaway purchase during the months of _____ or _____, 197__? Yes ____ No ____

2. Name of store _____

3. Item _____

4. Did you complete the purchase and get the item?
   Yes ____ No ____

5. If not, did you:

   a. Get a refund of any payments you made?
      Yes ____ No ____

   b. Apply any payments to the purchase of some other item?
      Yes ____ No ____

   c. Other? _____

Signed _____

Date _____

IN THE MATTER OF

TERRANCE D. LESKO, M.D.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-3031. Complaint, July 28, 1980—Decision, July 28, 1980

This consent order requires, among other things, a medical doctor affiliated with two California firms engaged in the sale of hair replacement services, to cease soliciting, selling or performing hair implants; or misrepresenting, in advertising or otherwise, the safety or effectiveness of the hair implant process in the treatment of baldness. Should Dr. Lesko engage in any hair replacement business during period specified in the order, he must expend at least $8,000 on corrective advertising warning consumers that "Hair Implants Are Unsafe." The order also requires that the respondent notify past hair implant customers that the process is unsafe and that they should seek prompt medical attention.

Appearances

For the Commission: *George E. Schulman* and *Anne B. Roberts.*

For the respondent: *Pro se.*

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that Terrance D. Lesko, M.D., an individual, hereinafter sometimes referred to as respondent, has violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. Respondent Terrance D. Lesko, M.D. is an individual and a medical doctor who was affiliated with Hair Extension of Beverly Hills, Inc. and Hair Extension, Inc. His address is 1737 Clarion Loop, Cannon Air Force Base, New Mexico.

PAR. 2. Respondent is now, and for some time last past has been engaged in performing hair replacement processes, operations and surgical procedures for the treatment of baldness, thinning hair or loss of hair, or for the replacement of lost hair, including a process or operation which is known as a "hair implant" or "dermis inversion" process ("the Hair Implant Process").

For the purpose of this complaint, the Hair Implant Process is

defined as a hair replacement product, process, operation or surgical procedure which involves the insertion or placement of (1) synthetic fibers or filaments which simulate hair or (2) non-living human hairs, into or under the scalp of the patient.

COUNT I

Alleging violation of Section 5 of the Federal Trade Commission Act, the allegations of Paragraphs One and Two are incorporated by reference herein as if fully set forth verbatim.

PAR. 3. Respondent maintains, and has maintained, a substantial course of business, including the acts and practices as hereinafter set forth, which are in or affect commerce, as "commerce" is defined in the Federal Trade Commission Act.

PAR. 4. In the course and conduct of his said business, respondent is now making, and has made representations, orally and in writing, directly and indirectly, in commerce as "commerce" is defined in the Federal Trade Commission Act, for the purpose of inducing, and which are likely to induce, the purchase of the Hair Implant Process in commerce.

PAR. 5. Respondent represents, orally and in writing, directly and indirectly, that the Hair Implant Process in general is safe and effective, and that the Hair Implant Process as performed by respondent or by his agents, representatives or employees is safe and effective for providing the purchaser with a natural looking head of hair, or for treating baldness, thinning hair or loss of hair, or for replacing lost hair, and will not result in medical complications or infections.

PAR. 6. In truth and in fact, the Hair Implant Process is not generally recognized as safe and effective, and is not performed in a safe and effective manner by respondent. The Hair Implant Process, both in general and as performed by respondent, does not result in a natural looking head of hair, and is not an effective method of treatment for baldness, thinning hair or loss of hair, or for the replacement of lost hair. The Hair Implant Process, both in general and as performed by respondent, results in medical complications and infections which may endanger the health of the purchaser.

Therefore, the making of the representations set forth in Paragraph Five were and are false, misleading, deceptive and unfair.

PAR. 7. There existed, at all times relevant hereto, no reasonable basis for making the representations set forth in Paragraph Five herein.

Therefore, the making of the representations as set forth in

Paragraph Five herein, without a reasonable basis constituted and now constitutes unfair or deceptive acts or practices.

PAR. 8. Respondent fails to disclose, either orally or in writing, directly or indirectly, that the Hair Implant Process, in general and as performed by respondent, is not a safe or effective method of treatment for baldness, thinning hair or loss of hair, or for the replacement of lost hair, and presents a high risk of infection or other medical complications which may endanger the health of the purchaser.

PAR. 9. In truth and in fact, the Hair Implant Process, both in general and as performed by respondent, is not generally recognized as a safe or effective method of treatment for baldness, thinning hair or loss of hair, or for the replacement of lost hair and presents a high risk of infection or other medical complications which may endanger the health of the purchaser.

Therefore, the failure to disclose that the Hair Implant Process is not a safe or effective method of treatment for baldness, thinning hair or loss of hair, or for the replacement of lost hair, and the failure to disclose that it presents a high risk of infection or other medical complications which may endanger the health of the purchaser, constitute unfair or deceptive acts or practices.

COUNT II

Alleging violation of Section 12 of the Federal Trade Commission Act, the allegations of Paragraphs One and Two are incorporated by reference herein as if fully set forth verbatim.

PAR. 10. In the course and conduct of his said business, respondent has disseminated and caused the dissemination of certain advertisements concerning the Hair Implant Process through the United States mails and by various means in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, including, but not limited to, the insertion of advertisements in magazines and newspapers with national circulations, and advertisements in the form of a brochure entitled "Hair TransCenter" which was, and is, sent through the United States mails, for the purpose of inducing, and which is likely to induce, the purchase of respondent's Hair Implant Process, and has disseminated and caused the dissemination of advertisements concerning said Hair Implant Process by various means, including but not limited to the aforesaid media, for the purpose of inducing and which are likely to induce, directly or indirectly, the purchase of said Hair Implant Process in commerce.

PAR. 11. Respondent represents directly and indirectly, in said

advertisements, disseminated as previously described, but not necessarily inclusive thereof, that the Hair Implant Process is a safe and effective method for providing the patient with a natural looking head of hair, or for treating baldness, thinning hair or loss of hair, or for replacing lost hair, and that the Hair Implant Process is approved by doctors, and will not result in medical complications or cause infections.

PAR. 12. In truth and in fact, the Hair Implant Process, both in general and as performed by respondent, is not a safe or effective method for the treatment of baldness, thinning hair or loss of hair, or for the replacement of lost hair. The Hair Implant Process presents a high risk of severe infections or other medical complications which may endanger the health of the purchaser. The Hair Implant Process is not an effective method of treatment for baldness, thinning hair or loss of hair, or for the replacement of lost hair, because the implanted hairs fall out or break off shortly after inserted. In addition, due to the Hair Implant Process, frequently a patient loses his own hair. The Hair Implant Process is not approved by doctors relying on competent and reliable scientific evidence, and in fact, generally is recognized by doctors as an unsafe and ineffective method of treatment for baldness, thinning hair or loss of hair, or for the replacement of lost hair.

Therefore, the advertisements referred to in Paragraphs Ten and Eleven, were and are misleading in material respects and constituted, and now constitute, false advertisements.

PAR. 13. In the course and conduct of his business, and at all times mentioned herein, respondent has been, and now is, in substantial competition in or affecting commerce with corporations, firms and individuals engaged in the sale of products and services of the same general kind and nature as the products and services sold by respondent.

PAR. 14. The use by respondent of the aforesaid false, misleading, and deceptive statements, representations, acts and practices, directly or by implication, has had, and now has, the capacity and tendency to mislead members of the public into the erroneous and mistaken belief that said statements and representations were, and are, true and complete, and into the purchase of substantial quantities of respondent's products and services by reason of said erroneous and mistaken belief.

PAR. 15. The acts and practices of respondent, as herein alleged, were and are all to the prejudice and injury of the public and of respondent's competitors and constituted, and now constitute, unfair methods of competition and unfair or deceptive acts or practices in

or affecting commerce in violation of Section 5 of the Federal Trade Commission Act. The acts and practices of respondents, as herein alleged, are continuing and will continue in the absence of the relief herein requested.

Decision and Order

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the Los Angeles Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act; and

The respondent, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint and waivers and other provisions as required by the Commission's Rules; and

The respondent agreed to provide to the Commission the names and addresses of his customers who underwent or paid money to undergo the Hair Implant Process and that the Commission may notify each said customer regarding the risks and problems involved in the Hair Implant Process and the fact that this order has been accepted by the Commission, such notice being substantially similar to the following letter:

Dear _____:

Hair Extension told us that you came to their office for hair implants. The FTC has reason to believe that the hair implant process is not safe or effective at the present time. There is no medically safe way to do hair implants. Many of their customers have developed scalp infections.

Hair Extension has promised the Federal Trade Commission that they will not do any more hair implants until the Food and Drug Administration approves a safe and effective procedure that protects future customers. However, we thought we should contact former customers to let them know the problems they could have with their implants.

Some people get infections right away. For others, an infection may develop months later. A few may never have a problem.

Many people report severe symptoms—pain, noticeable scarring, hairs breaking off,

scalp soreness, redness and swelling. However, others may have only a minor problem. A problem may not be too noticeable now but could develop into a more serious problem if not treated.

Therefore, for your own safety, you may want to see a doctor for an examination of your scalp and implants. If you do have any of these symptoms, you should go see a doctor immediately. The agreement which Hair Extension signed does not provide refunds or money for your doctor bills. However, you might want to contact an attorney to find out whether Hair Extension may be liable for any costs or injury you have suffered.

and, the Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further comformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Proposed respondent Terrance D. Lesko, M.D. is an individual and medical doctor who was affiliated with Hair Extension of Beverly Hills, Inc., 8383 Wilshire Boulevard, Beverly Hills, California and Hair Extension, Inc., 16152 Beach Boulevard, Huntington Beach, California. His address is 1737 Clarion Loop, Cannon Air Force Base, New Mexico.

Hair Extension of Beverly Hills, Inc., also trading and doing business as Hair TransCenter, is a corporation organized, existing and doing business under and by virtue of the laws of the State of California. Its principal office and place of business is at 8383 Wilshire Boulevard, Beverly Hills, California.

Hair Extension, Inc., also trading and doing business as Hair TransCenter, is a corporation organized, existing and doing business under and by virtue of the laws of the State of California. Its principal office and place of business is at 16152 Beach Boulevard, Huntington Beach, California.

Both corporations, as well as Lee Marlow and Ann Marlow, officers and directors of the corporations, previously signed an agreement containing consent order to cease and desist, which was accepted by the Commission on September 25, 1979. Dr. Lesko is Ann Marlow's brother.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

ORDER

For the purpose of this Order, the following definition shall apply:

The "Hair Implant Process" refers to any hair replacement product, process, operation or surgical procedure which involves the insertion or placement of (1) synthetic fibers or filaments which simulate hair or (2) non-living human hairs, into or under the scalp of a patient.

I

It is ordered, That Terrance D. Lesko, M.D., an individual, his agents, representatives, employees and persons under respondent's control, directly or through any corporation, subsidiary, division or other device, in connection with the advertising, offering for sale and sale of the Hair Implant Process, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended, do forthwith cease and desist from:

1. Disseminating, or causing or permitting the dissemination of any advertisement or other representation or claim, express or implied, that the Hair Implant Process is safe or effective in the treatment of baldness, thinning hair or loss of hair, or for the replacement of lost hair.
2. Soliciting, recommending, promoting, offering for sale, selling, arranging for or performing the Hair Implant Process.

Provided, however, that nothing shall prevent respondent from filing with the Commission a petition to modify this order, *provided* that respondent is able to demonstrate to the satisfaction of the Commission by competent and reliable scientific tests that:

1. The Hair Implant Process is safe and effective (and affirmative approval by the Food and Drug Administration that the process is safe and effective shall be deemed sufficient proof of compliance with this provision), and
2. The Hair Implant Process will be performed by respondent (or by persons recommended by or under the control of respondent) in a safe and effective manner (and affirmative approval by the Food and Drug Administration that named respondent will perform the Hair Implant Process in a safe and effective manner shall be deemed sufficient proof of compliance with this provision.)

Provided, however, that if the Commission determines, upon

proper application of respondent, that the Hair Implant Process is safe and effective and that the Hair Implant Process will be performed by respondent (or by persons recommended by or under the control of respondent) in a safe and effective manner, and such determination shall be based upon respondent's proof of compliance with the provisions set forth in the preceding paragraph, and if the Commission determines that further relief is necessary in the public interest, the Commission may require respondent to provide further relief. Said further relief may include, but is not limited to: (1) affirmative disclosures that there is a high probability of discomfort and pain and a high risk of infection, skin disease and scarring; that continuing special care is necessary to minimize the probabilities and risks referred to herein; and that such care may involve additional costs for medications and assistance; (2) a cooling-off period, following execution of contracts for services; and (3) a recommended consultation with an independent duly-licensed physician before undergoing the Hair Implant Process.

II

It is further ordered, That if Terrance D. Lesko, M.D., an individual, his agents, representatives, employees and persons under respondent's control, directly or through any corporation, subsidiary, division or other device, are engaged in or affiliated with any business which offers methods of treating baldness, loss of hair or thinning hair, or the replacement of lost hair, and if such business advertises in any media during a one year period commencing thirty (30) days after this order becomes final, then respondent shall disclose in such advertising during that one year period, clearly and conspicuously, in type no smaller than the smallest type otherwise in the advertising or 10 point type, whichever is larger, the following notice:

WARNING

Hair implants, using artificial hair or human hair, are medically unsafe. We do not use this procedure.

III

It is further ordered, That if Terrance D. Lesko, M.D., an individual, his agents, representatives, employees and persons under respondents' control, directly or through any corporation, subsidiary, division or other device, are engaged in any business which offers methods of treating baldness, loss of hair or thinning hair, or the

replacement of lost hair, during a one year period commencing thirty (30) days after this Order becomes final, respondents shall place the following advertisement in the *Los Angeles Times*, the *Santa Ana Register*, the *Los Angeles Herald Examiner* and *Los Angeles Magazine*.

HAIR IMPLANTS ARE UNSAFE

Hair implants, the inserting of synthetic hairs or human hairs into the scalp, are medically unsafe.

Many hair implant patients have developed scalp infections, noticeable scarring *and* have lost the implanted hair.

The *Federal Trade Commission* advises anyone considering a hair implant—or any other "cure" for baldness–to see a doctor. If you had a hair implant and have developed any problems, you should go see a doctor immediately.

This notice was prepared by the FTC and placed at the expense of Hair Extension, Inc., as part of a recent consent agreement between it and the FTC.

Federal Trade Commission
Los Angeles Regional Office

A. The placement of the advertisement in the newspapers shall be as follows:

1. Said advertisements shall appear at least once per month in each and every newspaper and magazine identified above, for six consecutive months commencing thirty (30) days after the date this order becomes final.
2. Said advertisement shall appear in the Sunday edition of each above-identified newspaper.
3. Respondent shall request placement of the advertisements in the Sports section of each newspaper.

B. The size of the advertisement shall be as follows:

1. The advertisement to be placed in the *Los Angeles Magazine* shall be equal to or larger than one column in width and the full length of the page.
2. The advertisement to be placed in the *Los Angeles Times, Santa Ana Register* and *Herald Examiner* shall be equal to or larger than two columns in width and four inches in length.

C. Respondent shall endeavor to obtain bulk rates for placing said advertisements at the lowest possible rates. Respondent shall spend no less than $8,000.00 for placing the advertisement required by this section.

D. The format, type size and type face of the advertisement shall

be subject to the approval by the Commission or its representative prior to its use by respondent.

IV

It is further ordered, That for a period of five (5) years from the effective date of this Order, respondent shall promptly notify the Commission of the discontinuance of his/her present business or employment and of his/her affiliation with a new business or employment which is engaged, during the time of such employment or affiliation, in methods of treating baldness, thinning hair, loss of hair or of the replacement of lost hair. Such notice shall contain respondent's current business address, a statement of the nature of the business or employment in which the respondent is newly engaged and a description of the respondent's duties and responsibilities in connection with the business or employment. The expiration of the notice provision of this paragraph shall not affect any other obligation arising under this Order.

It is further ordered, That respondent shall, within sixty (60) days after service upon them of this Order, and within thirty (30) days after termination of the advertising required by Section III of this Order, file with the Commission a report, in writing, setting forth in detail the manner and form in which they have complied with this Order.

IN THE MATTER OF

TOWLE MANUFACTURING COMPANY

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-3029. Complaint, July 29, 1980—Decision, July 29, 1980

This consent order requires, among other things, a Newburyport, Mass. manufacturer, importer and distributor of silver products to cease establishing, maintaining or enforcing any agreement or arrangement with its dealers that has the effect of fixing and enforcing resale prices for its products and conditioning retention of dealerships on adherence to suggested resale prices. The firm is prohibited from inducing dealers or prospective dealers to report those who fail to adhere to suggested resale prices and barred from taking adverse action against reported dealers. Materials containing resale pricing information must include a statement advising that dealers are not bound to listed prices. Respondent is further required to reinstate those dealers who were terminated for failing to comply with the firm's pricing policy and maintain a file containing specified data for a period of three years.

Appearances

For the Commission: *Harold F. Moody* and *William F. Connolly.*

For the respondent: *John R. Hally, Nutter, McClennen & Fish,* Boston, Mass.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that Towle Manufacturing Company, a corporation, hereinafter sometimes referred to as respondent, has violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. For purposes of this complaint the following definition shall apply:

"Dealer" means any person, partnership, corporation or other business entity who purchases Towle Manufacturing Company products for resale.

PAR. 2. Respondent Towle Manufacturing Company is a corporation organized, existing and doing business under and by virtue of

the laws of the Commonwealth of Massachusetts, with its office and principal place of business located at 260 Merrimac St., Newburyport, Massachusetts.

PAR. 3. Respondent has been and is now engaged in the manufacture, importation, distribution, and sale of silverware, plated ware and stainless steel ware including, but not limited to, sterling silver flatware and hollowware, silver plated and pewter hollowware, stainless steel flatware, cutlery, sterling silver jewelry, candlesticks, hurricane lamps, napkin rings, table trays and table mats. Said products are subsequently distributed and sold to dealers throughout the United States for resale to the general public. Gross sales by respondent for fiscal year 1976 exceeded $30,000,000.

PAR. 4. Respondent distributes and sells its products to dealers located in all fifty states and the District of Columbia, through salespersons and sales representatives who act under the direction and control and carry out the policies of respondent.

PAR. 5. In the course and conduct of its business as aforesaid, respondent causes and has caused said products to be shipped from the state in which they are manufactured to purchasers in other states. Respondent maintains, and at all times mentioned herein has maintained, a substantial course of trade in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended.

PAR. 6. Except to the extent that competition has been hampered, hindered, lessened or restrained as set forth in this complaint, respondent has been and is now in competition with other persons, firms, and corporations engaged in the manufacture, importation, sale, and distribution of sterling silver flatware and hollowware, silver plated and pewter hollowware, stainless steel flatware, cutlery, sterling silver jewelry, candlesticks, hurricane lamps, napkin rings, table trays and table mats in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended.

PAR. 7. Respondent, in combination, agreement or understanding with certain of its dealers, or with the cooperation or acquiescence of other of its dealers, has for the last several years been engaged in a course of action to fix, establish, and maintain certain resale or retail prices at which said products are resold to the general public. In furtherance of said course of action, respondent has for the last several years been engaged in the following acts and practices, among others:

(a) Establishing agreements, understandings or arrangements

with its dealers, as a condition precedent to the granting or retention of a dealership, that such dealers will sell respondent's products only at prices dictated by respondent;

(b) Informing certain of its dealers, by direct and indirect means, that respondent expects and requires such dealers to maintain and enforce certain resale or retail prices, or such dealerships will be terminated;

(c) Obtaining from its dealers cooperation and assistance in identifying and reporting dealers who advertise, offer to sell, or sell respondent's products at prices other than those dictated by respondent;

(d) Directing or requiring salespersons, sales representatives, and other employees or agents of respondent to secure and report information identifying dealers who advertise, offer to sell or sell respondent's products at prices below the prices established or suggested by respondent;

(e) Communicating with certain dealers who fail to sell respondent's products at those prices dictated by respondent and securing, or attempting to secure, assurances from such dealers that they will adhere to and observe those prices dictated by respondent;

(f) Threatening to terminate certain dealers who fail or refuse to observe and maintain the prices dictated by respondent, or who advertise respondent's products at resale prices below the prices established or suggested by respondent;

(g) Requiring certain of its dealers to agree not to sell or otherwise supply or furnish its products to other dealers; and

(h) Regularly furnishing dealers with price lists and supplements thereto containing resale prices for respondent's products.

PAR. 8. By means of the aforesaid acts and practices, respondent, in combination, agreement, or understanding with certain of its dealers and with the acquiescence of other of its dealers, has established, maintained and pursued a course of action to fix and maintain prices at which respondent's products will be resold.

PAR. 9. The aforesaid acts and practices of respondent have had the effect of hindering, lessening, restricting, restraining and eliminating competition in the resale and distribution of said products, and, thus, are to the prejudice and injury of the public, and constitute unfair methods of competition and unfair acts and practices in or affecting commerce, in violation of Section 5 of the Federal Trade Commission Act, as amended.

Decision and Order

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the Boston Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act; and

The respondent, its attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent Towle Manufacturing Company is a corporation organized, existing and doing business under and by virtue of the laws of the Commonwealth of Massachusetts, with its office and principal place of business located at 260 Merrimac St., in the city of Newburyport, Commonwealth of Massachusetts.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

Order

Definition

For purposes of this Order the following definition shall apply:

"Dealer" means any person, partnership, corporation or other business entity who purchases Towle Manufacturing Company products for resale.

I

It is ordered, That Towle Manufacturing Company, a corporation, its successors and assigns, and its officers, and respondent's agents, representatives and employees, directly or through any corporation, subsidiary, division or other device in connection with the manufacture, importation, distribution, offering for sale or sale of sterling silver flatware and hollowware, silver plated and pewter hollowware, stainless steel flatware, cutlery, sterling silver jewelry, candlesticks, hurricane lamps, napkin rings, table top trays, tabletop mats, or other products in or affecting commerce as "commerce" is defined in the Federal Trade Commission Act, as amended, do forthwith cease and desist from:

1. Entering into, maintaining, or enforcing any contract, agreement, understanding, arrangement, combination, or course of conduct which fixes, maintains, establishes, sets or enforces the price at which dealers sell any of respondent's products.

2. Requiring any dealer or prospective dealer to enter into any oral or written agreement or understanding that such dealer or prospective dealer will adhere to any resale price for any of respondent's products as a condition to receiving or retaining its dealership.

3. Refusing to sell or threatening to refuse to sell, either directly or indirectly, to any dealer or prospective dealer who desires to engage in the sale of respondent's products for the reason that such dealer will not enter into an understanding or agreement with respondent to advertise or sell any of respondent's products at only those prices established or suggested by respondent.

4. Securing or attempting to secure any promises or assurances, either directly or indirectly, from any dealer or prospective dealer regarding the prices at which such dealer will advertise or sell any of respondent's products, or requesting any dealer or prospective dealer, either directly or indirectly, to obtain approval from respondent for the price offered by said dealer in any advertisement for any of respondent's products.

5. Requesting or requiring any dealer or prospective dealer, either directly or indirectly, to report any dealer who does not sell any of respondent's products at any particular price, or acting on a report so obtained by refusing or threatening to refuse sales to any dealer so reported, or otherwise to discriminate against any such dealer.

6. Directing or requiring respondent's salesmen, or any other agents, representatives, or employees, directly or indirectly, to

report dealers who do not sell any of respondent's products for any particular price, or to act on such a report by refusing or threatening to refuse sales to any dealer so reported.

7. Refusing to sell or threatening to refuse to sell any of respondent's products to any dealer for the reason that said dealer had been reported as not adhering to or observing those prices established or suggested by respondent.

8. Requiring from any dealer charged with price cutting or failure to adhere to any particular price, either directly or indirectly, promises or assurances of the observance of any particular price as a condition precedent to future sales to said dealer.

9. Terminating, threatening, intimidating, coercing, delaying shipments, or taking any other action to prevent or hinder the sale of any of respondent's products by a dealer because said dealer has advertised or sold, is advertising or selling, or is suspected of advertising or selling any of respondent's products at other than prices that respondent has dictated.

10. Requiring or inducing by any means, any dealer or prospective dealer to refrain or to agree to refrain from reselling any of respondent's products to any other dealer.

11. Requiring, directly or indirectly, any dealer to resell to respondent any unsold stock of any of respondent's products in the event that business relations between respondent and the dealer are terminated; provided that respondent shall not be prohibited from repurchasing such unsold stock with the consent of the dealer, or where respondent has a "security interest" in said products or where the dealer is unable to meet its financial obligations to the respondent.

12. Publishing, disseminating, circulating or providing by any other means, any resale price for any of respondent's products unless it is clearly and conspicuously stated on each page of any price list, book, tag, advertising or promotional material or other document that the price is "suggested" and that the dealer is free to sell respondent's products at whatever price he chooses.

II

It is further ordered, That respondent herein shall, within thirty (30) days after service upon it of this Order, mail or deliver, and obtain a signed receipt therefor, a copy of this Order to every present dealer, to every dealer terminated by respondent since January 1, 1974, unless respondent can establish that the dealer terminated did not at the time of termination have good credit or reasonably

adequate facilities for selling respondent's products, and for a period of three (3) years from the date of service of this Order, to every new dealer within ten days of receipt of the first Order from said dealer, under cover of the letter annexed hereto as Exhibit A.

III

It is further ordered, That respondent shall within sixty (60) days from the date of service of this Order, mail or deliver and obtain a signed receipt therefor, a written offer of reinstatement, upon the same terms and conditions available to respondent's other dealers, to any dealer who was terminated by respondent from January 1, 1974, to the date of service of this Order, unless respondent can establish that the applicant does not or did not at the time of termination have good credit or that the dealer does not have reasonably adequate facilities for selling respondent's products, and forthwith reinstate any such dealer who within thirty (30) days thereafter requests, in writing, reinstatement.

IV

It is further ordered, That respondent herein shall within thirty (30) days of service upon it of this Order, distribute a copy of this Order to each of its operating divisions and subsidiaries and to all officers, sales personnel, sales agents and sales representatives, and secure from each such entity or person a signed statement acknowledging receipt of said Order.

V

It is further ordered, That respondent:

1. Notify the Commission at least thirty (30) days prior to any proposed change in the respondent such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other such change in the corporation which may affect compliance obligations arising out of the Order.

2. For a period of three (3) years from the date this Order becomes final, establish and maintain a file of all records referring or relating to respondent's refusal during such period to sell its products to any dealer, which file shall contain a record of a communication to each such dealer explaining respondent's refusal to sell, and which file will be made available for Commission inspection on reasonable notice.

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VI

It is further ordered, That the respondent herein shall, within sixty (60) days after service upon it of this Order, file with the Commission a report in writing setting forth in detail the manner and form in which it has complied with the Order.

EXHIBIT A

(Letterhead of Towle Manufacturing Company)

Dear Dealer:

Towle Manufacturing Company has entered into an agreement with the Federal Trade Commission relating to the distributional activities and pricing policy of Towle. A copy of the consent order entered into pursuant to that agreement is enclosed herewith.

Towle has entered into this agreement solely for the purpose of settling a dispute with the Commission, and the agreement and consent order is not to be construed as an admission by Towle that it has violated any of the laws administered by the Commission, or that any of the allegations in the complaint are true and correct. Instead, the order merely relates to the activities of Towle in the future.

In order that you may readily understand the terms of the consent order, we have set forth the essentials of the agreement with the Commission, although you must realize that the consent order itself is controlling rather than the following explanation of its provisions:

(1) Our dealers are free to set their own resale prices for our products.

(2) Towle will not solicit, invite or encourage dealers, or any other persons to report any dealer not following any resale price for any of said products, and, furthermore, will not act on any such reports sent to it.

(3) Towle will not require or induce its dealers to refrain from advertising said products at any price or from selling or offering said products at any prices to any person.

Sincerely yours,

Edward W. Mulligan
President

Enclosure

IN THE MATTER OF

KELLOGG COMPANY, ET AL.

Docket 8883. Interlocutory Order, July 31, 1980

DENIAL OF MOTION TO DISQUALIFY ADMINISTRATIVE LAW JUDGE BERMAN

ORDER

The Commission has before it a variety of motions and requests filed by respondents, including: (i) the motion of respondent Kellogg Company ("Kellogg"), dated July 20, 1979, for reconsideration of the Commission's Order dated December 8, 1978, in which the Commission concluded that Administrative Law Judge Harry R. Hinkes became "unavailable" within the meaning of 5 U.S.C. 554(d) (1976) upon his retirement on September 8, 1978; (ii) Kellogg's motion, dated January 31, 1980, to disqualify Administrative Law Judge Alvin L. Berman from presiding in this proceeding and for related discovery, which was certified to the Commission by Judge Berman on February 12, 1980; (iii) the request of respondent General Mills, Inc. ("General Mills"), dated April 3, 1980, for discovery and an evidentiary hearing regarding the "unavailability" of Judge Hinkes; (iv) Kellogg's request, dated April 3, 1980, that the Commission rescind its December 8, 1978, Order and direct a retrial of this proceeding or, in the alternative, that the Commission order an evidentiary hearing and allow depositions of 21 persons, and that an ALJ not currently employed by the Commission be appointed to preside over such proceedings; and (v) the motion of General Foods Corporation ("General Foods") dated April 3, 1980 for dismissal of the complaint, which allegedly is required "as a result of the Commission's actions in connection with the retirement and contractual reemployment of former Administrative Law Judge Harry R. Hinkes."[1]

After reviewing the relevant procedural history, we shall first consider Kellogg's motion to disqualify Judge Berman and shall then turn to the various issues raised by Kellogg's July 20, 1979, motion for reconsideration of the Commission's Order of December 8, 1978, and the respondents' April 3, 1980, motions and requests.

[1] In addition, on June 9, 1980, Judge Berman certified to the Commission the question of whether he had authority to establish a briefing schedule in the principal proceeding on the merits while the Commission conducted the inquiry into the circumstances of Judge Hinkes' retirement. We agree with Judge Berman that the Commission's inquiry is collateral to the merits, and we affirm his authority to adopt the briefing schedule he has decided upon. We also grant his request for an extension of the time within which the initial decision may be filed.

I.

The complaint, charging the respondents with engaging in unfair methods of competition in violation of Section 5 of the FTC Act, 15 U.S.C. 45 (1976), was issued on April 26, 1972. The proceeding was assigned to ALJ Harry R. Hinkes, who presided over all pre-trial proceedings and a substantial portion of the trial, including all of complaint counsel's case-in-chief and much of the case-in-defense of Kellogg and General Mills. In all, Judge Hinkes presided over some four years of pretrial proceedings and some 243 hearing days encompassing more than 30,000 pages of transcript.

On August 16, 1978, Chief ALJ Daniel H. Hanscom submitted to Chairman Pertschuk a memorandum stating that Judge Hinkes had advised that he intended to retire as of August 31, 1978. Judge Hanscom recommended that Judge Hinkes be retained under contract to complete the case. His recommendation and surrounding events are the subject of the pending motions, but it is undisputed that Judge Hinkes did retire on September 8, 1978, and that he continued to preside over this case until October 20, 1978, under contract.

On September 22, 1978, Kellogg filed a motion, subsequently joined in by General Mills, for discovery concerning the contract, which Judge Hinkes certified to the Commission. Thereafter, all three respondents moved for disqualification of Judge Hinkes, and on October 20, 1978, the Commission stayed further proceedings before the ALJ. Complaint counsel subsequently petitioned for Judge Hinkes' removal. On December 8, 1978, Chairman Pertschuk, after considering the objections raised by respondents, concluded that the contract was "of questionable validity" and that he would not submit the contract to the Civil Service Commission for approval. On the same date the Commission issued an Order holding that, under the circumstances, Judge Hinkes had become "unavailable" within the meaning of 5 U.S.C. 554(d) (1976) as of the date of his retirement.

The Commission remanded the case for appointment of a new ALJ, and ALJ Alvin L. Berman was appointed. The Commission also instructed the parties to brief within 45 days certain issues relating to the need for a trial *de novo* "as well as any other legal or factual matters that the submitting party may deem relevant to the issue of whether retrial is required and, if so, to what extent." In their memoranda filed in response to this direction, none of the respondents sought reconsideration of the December 8, 1978, Order or challenged the Commission's determination of Judge Hinkes' un-

availability. On May 24, 1979, Judge Berman issued his order holding that a retrial of the merits was not required.

On July 20, 1979, Kellogg moved for (i) reconsideration of the Commission's December 8 Order holding Judge Hinkes had become "unavailable," and (ii) an evidentiary hearing concerning the circumstances of Judge Hinkes' retirement.[2] By Order of November 13, 1979, the Commission reserved decision on Kellogg's request for reconsideration of the December 8, 1978, Order, and instituted a limited inquiry into the circumstances surrounding Judge Hinkes' retirement. The Commission explained that "both the resolution of Kellogg's motion for reconsideration and the public interest generally would be served by an inquiry into the facts of Judge Hinkes' retirement as they relate to Kellogg's allegations of impropriety", *i.e.,* that "the agency itself [had brought] about the unavailability of the ALJ." Specifically, the Commission directed Chief Judge Hanscom, Deputy Chief Judge Ernest Barnes, and Deputy Executive Director Barry Kefauver to file affidavits setting forth "their knowledge of the circumstances of Judge Hinkes' retirement and the negotiations leading to the execution of the contract with Judge Hinkes and, in particular, their recollections of the time, place, and substance of any conversations with Judge Hinkes regarding either his desire to retire or his desire to continue as an ALJ if he could move to Los Angeles." The Commission noted that Chairman Pertschuk's recollections concerning his role and that of his staff had been memorialized and appended to the December 8, 1978, Order. Finally, the Commission directed the Secretary to send to Judge Hinkes a letter requesting that he file an affidavit setting forth his recollection of the circumstances.

In issuing its November 13, 1979, Order, the Commission anticipated that Judge Berman would preside over the inquiry into the circumstances surrounding Judge Hinkes' retirement. However, Judge Berman recused himself from presiding over this inquiry, stating that "while I feel that I am able to comply with the Commission's directive in an impartial manner, I am aware that my impartiality may reasonably be questioned." Furthermore, Chief Judge Hanscom advised the Commission that the concerns expressed by Judge Berman applied to all of the other Commission ALJs. Accordingly, on November 30, 1979, the Commission issued an Order providing that the Commission itself would conduct the inquiry into the circumstances surrounding Judge Hinkes' retirement.

[2] Kellogg's motion also sought interlocutory review of Judge Berman's decision respecting the need for retrial of this proceeding and a stay of the proceeding. Both requests were denied by the Commission in its Order of November 13, 1979.

On January 31, 1980, Kellogg moved to disqualify Judge Berman from presiding over the principal proceeding on the merits, arguing that (i) "because Judge Berman has conceded he was a friend of ALJ Hinkes, his continued participation in any aspect of the case would present an appearance of impropriety"; (ii) that Judge Berman could not properly "partially recuse himself from this case"; and (iii) that Judge Berman should be disqualified because he was selected to replace Judge Hinkes by Judge Hanscom, who "may have selected Judge Berman * * * on the understanding that Judge Berman not allow * * * a retrial [of the case]." Judge Berman denied the requested relief, and certified Kellogg's motion to the Commission; in the certification Judge Berman discussed in detail his relationship to Judge Hinkes, his reasons for recusing himself from the inquiry into the circumstances surrounding Judge Hinkes' retirement, and the circumstances of his assignment to this proceeding.

In the meantime, in December 1979, Judges Hanscom and Barnes and Mr. Kefauver filed their affidavits as directed by the Commission. In lieu of an affidavit, Judge Hinkes submitted a statement taken under oath before Commissioner Clanton. Subsequently, the Commission issued an Order (i) directing that the transcript of Judge Hinkes' statement be placed in the record in this proceeding, and (ii) directing the parties to file within 30 days "their views on whether additional fact-finding is needed as to the circumstances surrounding Judge Hinkes' retirement and subsequent reemployment under contract, and if so, by what procedure such fact-finding should be undertaken."

On April 3, 1980, each of the respondents filed a motion or request with the Commission. (1) General Mills argued for further discovery and an evidentiary hearing—specifically, General Mills sought the depositions of Judges Hanscom, Barnes and Hinkes and Mr. Kefauver; Charles Dullea, former Director of the Office of Administrative Law Judges of the Civil Service Commission; Chairman Pertschuk; and eight other present or former Commission employees. General Mills also requested that, after the depositions were taken, an evidentiary hearing be held before an ALJ from another agency designated by the Civil Service Commission. (2) Kellogg requested that the Commission order a complete retrial of this case. In the alternative, Kellogg requested (i) that Judges Hanscom, Barnes and Hinkes and Mr. Kefauver testify at an evidentiary hearing; (ii) that Kellogg be permitted to depose 21 people (principally present or former Commission employees, including all of the persons General Mills wishes to depose); and (iii) that an ALJ not currently employed by the Commission be appointed to preside over

such proceedings. (3) General Foods moved for dismissal of the complaint, alleging that the Commission's actions in connection with the retirement and reemployment of Judge Hinkes had deprived General Foods of due process of law in three respects: (i) by conducting *ex parte* negotiations with a sitting judge leading to an illegal contractual arrangement; (ii) by impermissibly intermingling its prosecutorial, administrative and judicial functions; and (iii) by inducing Judge Hinkes to retire through the offer of an illegal contract.

II.

In support of its motion to disqualify Judge Berman, Kellogg argues "that the facts concerning Judge Berman's admitted friendship with ALJ Hinkes which created an appearance of impropriety necessitating his withdrawal from the proceedings for the supplementation of record also compel Judge Berman's recusal from the remainder of the * * * case" (Kellogg Memorandum filed Feb. 20, 1980, at 3). Kellogg also argues "that an ALJ may not recuse himself from part of an adjudicative proceeding, so that two triers of fact must then preside concurrently over the reception of evidence in different portions of that proceeding." This argument in turn rests on three separate contentions: (a) that neither the Administrative Procedure Act nor the Commission's Rules of Practice for Adjudicative Proceedings permit two triers of fact to preside simultaneously over different portions of the same case; (b) that such a procedure also violates basic principles of due process; and (c) that analogous cases dealing with judicial disqualification prohibit a judge from recusing himself partially from an ongoing case. Finally, Kellogg argues that Judge Berman's disqualification is compelled by the fact that he was assigned to the case by then-Chief Judge Hanscom, who was himself disqualified by virtue of his role in recommending to Chairman Pertschuk that the Commission offer a contract to Judge Hinkes.

A. Kellogg contends that Judge Berman's friendship with Judge Hinkes disqualifies him from any aspect of the case. Assuming, as does Kellogg, that Judge Berman's future participation in this case is to be determined by a standard that would disqualify Judge Berman upon the existence of an "appearance of impropriety," we do not find Judge Berman disqualified from presiding over the trial of the merits of this case.

The determination of whether events have created an "appearance of impropriety" can be difficult; however, certain benchmarks have

evolved. Our role in passing on Judge Berman's participation is to ask "whether a reasonable person would have had a reasonable basis for doubting the Judge's impartiality. * * * Neither our faith nor the imaginings of one highly suspicious of others are relevant. The inquiry begins and ends with whether a reasonable person would have had a reasonable basis for doubting the Judge's impartiality." *Rice* v. *McKenzie,* 581 F.2d 1114, 1116–17 (4th Cir. 1978) (footnotes omitted); accord, *United States* v. *Cowden,* 545 F.2d 257, 265 (1st Cir.), *cert. denied,* 430 U.S. 909 (1977).

In our view, a reasonable person would conclude that Judge Berman's relationship with Judge Hinkes does not call Judge Berman's impartiality into doubt. No rule of law disqualifies a judge from reviewing or reconsidering another judge's order because the two judges are acquaintances and colleagues. With respect to the substantive case, Judge Berman has been, and no doubt will continue to be, called upon to pass upon the prior rulings of Judge Hinkes. In the proceedings concerning Judge Hinkes' retirement, on the other hand, Judge Berman was apparently concerned that he might have had to judge the personal credibility of Judges Hinkes, Hanscom and Barnes:[3]

> I had in mind the possibility of being required to determine whether or not to subpoena the various individuals involved and the necessity to rule on the scope of examination and cross-examination of such individuals, as well as rulings that might be required with regard to particular objections that might be raised as to particular questions. In addition, there was the requirement to make factual findings with respect to possibly conflicting testimony on the part of [former Chief Judge Hanscom, Chief Judge Barnes, and Judge Hinkes]. I did not believe it appropriate for me to preside at such an inquiry. This was my thinking when I recused myself and these considerations are encompassed in the more general statement of reasons for recusement in my notice of November 21, 1979. [Certification and Denial Order at 3.]

There is of course a great deal of difference—in perception as well as fact—between reviewing the work of an acquaintance in a professional capacity and judging the personal credibility of fellow judges.[4] Judge Berman has described his relationship with Judge Hinkes–apparently they were merely colleagues, not even close friends; to require disqualification under such circumstances would be unprecedented, and if applied as a general rule would make

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[3] We intimate no view as to whether Judge Berman was required to withdraw from the proceedings concerning Judge Hinkes' retirement. Clearly, it was his right to do so whether or not he was disqualified. 5 U.S.C. 556 (1976). "Judges from time to time elect not to try cases, which they are sure that can try fairly and effectively, because of their concern to avoid any substantial doubt which circumstances beyond their control may create in the public mind about the impartiality of their administration of justice in the matters at hand." *Green* v. *Murphy,* 259 F.2d 591, 595 (3d Cir. 1958) (*en banc*) (Hastie, J. concurring).

[4] It is reported that "Judge Learned Hand considered it appropriate to review decisions of his cousin Judge Augustus Hand, when the former was a circuit judge and the latter a district judge." J. Frank, *Disqualification of Judges: In Support of the Bayh Bill,* 35 J. Law & Contemp. Prob. 43, 48 n.25 (1970).

administration of the federal courts and administrative agencies difficult, if not impossible. We do not believe that disqualification of Judge Berman is required and we so hold.

B. We turn now to Kellogg's contentions that the hearing procedures employed by the Commission are impermissible under the APA and the Commission's Rules, and deny due process, because of the simultaneous use of two triers of fact; and violate an alleged rule against partial recusals applicable to judicial disqualification. These contentions are addressed to the procedures employed by the Commission, rather than to the participation of Judge Berman, and they would seem to preclude the appointment of *any* ALJ in Judge Berman's stead.[5] But in any event, assuming *arguendo* that these objections are properly raised in a motion to disqualify the ALJ, we find them to be without merit.

1. Kellogg's arguments based on the APA and the Commission's Rules of Practice stem from its perception of the proceeding concerning Judge Hinkes' retirement as an "integral part" of the case on the merits. We cannot agree. In our view, the inquiry concerning the circumstances of Judge Hinkes' retirement is "distinct and separable" from the proceedings on the merits of the Commission's complaint. *Gasoline Prods. Co.* v. *Champlin Ref. Co.*, 283 U.S. 494, 500 (1930). The proceedings involve different witnesses and testimony, bearing upon different legal and factual issues. Most importantly for purposes of Kellogg's motion, Judge Berman's reasons for recusing himself from the proceedings concerning Judge Hinkes' retirement are entirely unrelated to his ability to judge the merits of the complaint.

Neither the APA, nor the Commission's Rules preclude "bifurcation" of a proceeding under the special circumstances of this case. Both the APA and the Commission's Rules contemplate that, in the ordinary case, all of the evidence bearing upon the merits of the complaint will be taken before an ALJ, who will write the initial decision. Judge Berman has not, however, excused himself from hearing any evidence going to the merits of the complaint, and his ability to write an initial decision is not compromised by his decision not to preside over the collateral inquiry concerning Judge Hinkes' retirement.[6]

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[5] Kellogg argues that the Commission should request an outside ALJ to replace Judge Berman (Kellogg Memorandum dated January 31, 1980 at 23), but "bifurcation" of the proceedings would appear no less objectionable merely because an outside ALJ was presiding over the trial on the merits.

[6] This case is thus distinguishable from *Channel 16 of Rhode Island, Inc.* v. *FCC*, 229 F.2d 520 (D.C. Cir. 1956), where the FCC defined six issues to be resolved in passing on the merits of a proceeding before it. The first five were issues of fact; the sixth issue was the appropriate ultimate legal conclusion flowing from resolution of the first five issues. The FCC referred the first five issues to a hearing examiner for an initial decision, but reserved the sixth issue to itself. With little discussion or analysis, the court held that this procedure was inconsistent with the

(Continued)

Within constitutional and statutory limitations, the formulation of procedures is generally within the discretion of the agency. *Vermont Yankee Nuclear Power Corp.* v. *NRDC,* 435 U.S. 519, 524–25 (1978). The Supreme Court has recognized "the general principle that '[i]t is always within the discretion of a court or an administrative agency to relax or modify its procedural rules adopted for the orderly transaction of business before it when in a given case the ends of justice require it. The action of either in such a case is not reviewable except upon a showing of substantial prejudice to the complaining party.' " *American Farm Lines* v. *Black Ball Freight Serv.,* 397 U.S. 532, 539 (1970) (quoting *NLRB* v. *Monsanto Chem. Co.,* 205 F.2d 763, 764 (8th Cir. 1953)). This rule is applicable to the special circumstances of this case, as respondents have not been prejudiced by the procedures adopted by the Commission. It is clear, for example, that, under both the APA (5 U.S.C. 556(b))[7] and the Commission's Rules (16 C.F.R. 3.42(g)) the Commission itself may conduct proceedings to resolve a motion to disqualify an ALJ—thus permitting two triers of fact in what is, in form, a single proceeding. See *Attorney General's Manual on the Administrative Procedure Act* 73 (1947). In this case, the inquiry into the circumstances of Judge Hinkes' retirement was prompted, initially by respondents' objections to Judge Hinkes' further participation in the proceeding, which sought, *inter alia,* a hearing under Commission Rule 3.42(g). Since the procedures adopted by the Commission are consistent with the APA and the Commission's Rules, we believe that the Commission has not exceeded its discretion by deciding to conduct itself the inquiry into the circumstances of Judge Hinkes' retirement.[8]

2. Kellogg's constitutional claim is equally without merit. Kellogg relies upon *Gasoline Prods., Inc.* v. *Champlin Ref. Co., supra,* a

requirements of 47 U.S.C. 409(b), noting that the hearing examiner was not "unavailable" to the FCC for purposes of the sixth issue. Here, in contrast, the issues being addressed by the Commission are collateral to, and independent of, the issues pertaining to the merits of the complaint; Judge Berman was "unavailable" to preside over the proceeding to resolve those issues; and the statutory provision on which the *Channel 16* court relied is inapplicable.

[7] 5 U.S.C. 556(b) (1976) provides: "On the filing in good faith of a timely and sufficient affidavit of personal bias or other disqualification of a presiding or participating employee, the agency shall determine the matter as a part of the record and decision in the case."

[8] The case law supports the proposition that an inquiry such as the inquiry into the circumstances of Judge Hinkes' retirement is collateral to, and independent of, the inquiry on the merits, and may be conducted by a different decisionmaker. For example, in *United Air Lines, Inc.* v. *CAB,* 281 F.2d 53 (D.C. Cir. 1960), a claim of improper *ex parte* communications was raised on review of CAB orders. The court, after considering and rejecting all of the substantive objections to the orders raised by the petitioners, nevertheless remanded for the CAB to conduct an inquiry into the *ex parte* allegations in order "to preserve the integrity of its own administrative process • • • ." *Id.* at 58. After the remand, the court sustained the procedures adopted by the CAB, specifically noting (with apparent approval) that the inquiry had been conducted "before a new examiner" appointed by the CAB, who issued an initial decision (later affirmed by the CAB) limited to the *ex parte* issues. *United Air Lines, Inc.* v. *CAB,* 309 F.2d 238, 239 (D.C. Cir. 1962). The court's actions in resolving the substantive objections and ordering a remand on the limited question of *ex parte* communications, and its affirmance of the "bifurcated" procedures adopted by the CAB, implicitly support our view that the procedures adopted in this case are proper, and implicitly reject Kellogg's contention that bifurcation is unallowable.

Seventh Amendment case involving the right to trial by jury in civil cases. The Court held that a partial retrial, to be permissible, must be on an issue "so distinct and separable from the others that a trial of it alone may be held without injustice." 283 U.S. at 500. There is, of course, no Seventh Amendment right to a jury trial in a Commission proceeding. But in any event, as noted above, we believe that the issues in the proceeding relating to Judge Hinkes' retirement meet this test.

Kellogg hypothesizes that the Commission may have entered into the contract with Judge Hinkes to avoid a retrial at a time when economic thought allegedly has shifted away from the theory of the complaint. It argues that it is entitled to present evidence of the Commission's conduct to the trier of fact in the merits proceeding as a type of admission by conduct supporting negative inferences. There is not a scintilla of evidence in the record to support the premise of Kellogg's argument, which is contrary to the presumption of administrative regularity. We believe Kellogg's rights are fully preserved by the procedures adopted by the Commission.

3. Kellogg additionally claims that statutes and case law concerning disqualification of judges do not permit partial recusal. The statutes are not directly applicable and the case law does not support Kellogg's broad contention. Judge Berman has not partially withdrawn from the case, but rather has wholly withdrawn from presiding over a separate inquiry involving distinct factual and legal issues. Although partial recusal may be improper if it is inconsistent with the reasons offered for recusal,[9] or may be precluded by statute,[10] the cases recognize the propriety of partial recusal where the basis of recusal is inapplicable to a segregable portion of a case. See, *e.g., Warner* v. *Rossignol,* 538 F.2d 910, 913 n.6 (1st Cir. 1976); *Middletown Nat. Bank* v. *Toledo A.A. & N.M.R. Co.,* 105 F. 547 (S.D.N.Y. 1900); *Coastal Petroleum Co.* v. *Mobil Oil Corp.,* 378 So.2d 336, 337 (Fla. App. 1980); *State* v. *Wilson,* 362 So.2d 536 (La. 1978); *Flannery* v. *Flannery,* 452 P.2d 846, 849 (Kan. 1969). In this case, Judge Berman's reasons for recusal from the inquiry into Judge

[9] See *Stringer* v. *United States,* 233 F.2d 947 (9th Cir. 1956), where the court, holding that on the facts before it the district judge, having disqualified himself on his own motion, could not resume control and try the case, nevertheless recognized:

> There may be some other instances where a judge could resume direction or even decide the issues. For instance, he might be mistaken as to the identity of a party. But the reason for resuming control should be more than a second reflection on the same facts which the trial judge considered originally disqualified him. [*Id.* at 948 n.2.]

[10] Thus, although the court in *State ex rel. Stefonick* v. *District Court,* 117 Mont. 86, 157 P.2d 96, 99 (1945), suggested, *in dictum,* a broad rule against partial disqualification, it found it "unnecessary to consider [the] question, since the statute does not make it possible to disqualify judges in particular portions of a cause or proceeding * * *." 157 P.2d at 99. No such statute applies in this case.

Hinkes' retirement would not deny respondents a fair hearing on the merits of the complaint. Accordingly, we find no reason to alter our conclusions, expressed above, that the procedures adopted by the Commission do not exceed applicable constitutional or statutory limitations, and are within the Commission's discretion.

C. Kellogg further argues that Judge Berman should be disqualified because he was assigned to the case by then-Chief Judge Hanscom. Kellogg contends that Judge Hanscom was disqualified from exercising that authority by virtue of his earlier involvement in the efforts to retain the services of Judge Hinkes. Kellogg asserts that this set of circumstances creates an appearance of impropriety requiring disqualification of Judge Berman, arguing that "one who knowingly sanctions the finalization of an unlawful contract * * * i[s] also likely to have selected an ALJ to complete [the] case whom he believed to be inherently predisposed to deny the respondents' request for a hearing *de novo*" (Kellogg Memorandum of Feb. 20, 1980, at 15). We reject this contention.

There is not the slightest record suggestion of any irregularity in Judge Berman's appointment. In the absence of any record evidence to the contrary, the Commission assumes, as it must, that the appointment was regular in every respect and conformed to legal requirements. This presumption is confirmed by the limited record evidence–Judge Hanscom advised Judge Berman that "he was 'up' for the next assignment under the rotation system maintained by the Office of the Administrative Law Judges." Certification and Denial Order at 4. Accordingly, in light of the speculative and unsupported nature of Kellogg's claims, its request for discovery into the circumstances of Judge Berman's appointment is denied.

Even assuming *arguendo* that Judge Hanscom would be disqualified from presiding over the adjudicative proceedings, it is clear under judicial and Commission precedent that he could appoint a successor to Judge Hinkes. In *Stringer* v. *United States,* 233 F.2d 947, 948 (9th Cir. 1956), a trial judge recused himself from a proceeding, which he then assigned to a judge of another division. Later, the case was transferred back to the original judge who resumed control of the case with the parties' consent and decided the merits. Although the Court of Appeals held that it was improper for the original judge to resume control of the case, it concluded that it was not improper for him to perform "the mechanical duties of transferring the case to another judge or other essential ministerial duties short of adjudication." Accord, *In re Application of Scott,* 397 F. Supp. 622, 624 (S.D. Tex. 1974) (citing cases). Analogous Commission precedent holds that a non-participating adjudicative decisionmaker may engage in the

administrative decision of whether to seek to retain an ALJ as a retired annuitant. *The Hearst Corp.*, 81 F.T.C. 1028, 1029 (1972). Thus, even assuming that Judge Hanscom would have been disqualified from the adjudicative proceeding, his appointment of Judge Berman was regular and proper.

III.

We shall next consider the issues raised in respondents' April 3, 1980, submissions and in Kellogg's July 23, 1979, motion for reconsideration.[11]

A. Kellogg advances five theories under which it seeks reconsideration by the Commission of its determination of Judge Hinkes' unavailability; by way of relief, Kellogg asks for a retrial, or, alternatively, for discovery and an evidentiary hearing. General Mills asks for discovery and an evidentiary hearing under a theory that closely resembles Kellogg's third theory, discussed *infra* .

1. Kellogg's first and second theories (in the order which Kellogg advances them in its April 3 memorandum) center on the time after the Commission entered into the contract with Judge Hinkes. The first theory hypothesizes that the contract was valid, Kellogg arguing that therefore the Commission had no right *not* to proceed with it. The second theory hypothesizes that the only missing element was the approval of the Civil Service Commission, and that the Commission had a duty to present the contract to the Civil Service Commission for its approval.

In advancing these arguments, Kellogg ignores the procedural posture in which the determination not to go forward with the contract was made, and misconstrues the basic applicable legal principles. As a matter of Commission organization, determinations on whether to retain an ALJ after retirement are within the administrative authority of the Chairman. *The Hearst Corp.*, 81 F.T.C. 1028, 1029 (1972). Accordingly, it was the Chairman who decided to proceed with a contractual arrangement with Judge Hinkes. Separate Statement of Chairman Pertschuk, Dec. 8, 1978, at 1. Having been advised that the contract was legal and that it had been cleared by the Civil Service Commission, the Chairman authorized the contract to further "the potential benefit to all concerned" (*id.* at 1–2).

[11] By a supplemental motion filed July 21, 1980, Kellogg argues that Chairman Pertschuk's Memorandum dated July 18, 1980, by which he recused himself from participating in the pending motions and requests regarding the contract with Judge Hinkes and the alleged need for further factfinding, affords an additional reason for reconsideration of the Commission's order of December 8, 1978. We have reconsidered that order, but for the reasons set forth herein as well as in that order, we reaffirm the order of December 8, 1978.

Subsequently, all three respondents and complaint counsel sought Judge Hinkes' removal from the case. "After reviewing the briefs of the parties," the Chairman concluded that there existed "substantial legal questions" about the validity of the contract. *Id.* at 3. "In light of * * * the fact that none of the parties desire[d] to have Judge Hinkes continue to preside and * * * all [were] willing to forego the benefits of having him continue," the Chairman determined not to seek Civil Service Commission approval. *Id.* Kellogg argues that the Commission at that time had no option but to continue with the contract. In essence, Kellogg contends that the Commission was bound to deny the motions filed by respondents and complaint counsel and proceed with the allegedly unlawful contract. Nothing in Section 5(c) of the APA, 5 U.S.C. 554(d) (1976), its legislative history, the relevant case law, or common sense requires such a bizarre result. Section 554(d) of the APA requires that the ALJ who heard the evidence make the initial decision, unless he or she becomes "unavailable". It imposes no duty on the agency to preserve an ALJ's availability. Here, the parties attacked as unlawful the Commission's attempt to retain Judge Hinkes under contract after his retirement, and demanded his removal. The statute does not require an agency to court error by doggedly pursuing an arrangement which the parties insist is improper and unlawful.[12]

Gamble-Skogmo, Inc. v. *FTC,* 211 F.2d 106 (8th Cir. 1954), is instructive. In that case, the Commission refused to attempt to have a statutorily retired ALJ's eligibility restored, over the objections of the respondent. The Court held that the Commission had not violated Section 554(d). *A fortiori,* the Commission's action here, where all respondents argued strenuously that the Commission was under a duty *not* to proceed with the contract, cannot be said to have been improper.

Finally, such a result seems dictated by pragmatic considerations. After the contract had been negotiated, the parties raised serious questions about its validity. Docket 8883 has been a long, complicated case involving a massive record, including the testimony of scores of witnesses and many exhibits. Because the parties raised serious questions about the validity of Judge Hinkes' service under the contract, the Chairman decided not to run the risk of proceeding with the contract. Since all parties appeared to favor Judge Hinkes'

[12] The Attorney General's Committee on Administrative Procedure, whose recommendations largely formed the basis of the APA, discussed the problem of substitution of ALJ's. It is clear from the Committee's report that the Committee thought that substitution could take place on consent of the parties. See Final Report of the Attorney General's Committee on Administrative Procedure at 50. See *United States* v. *L.A. Tucker Truck Lines, Inc.*, 344 U.S. 33, 37–38 (1952).

removal, the Chairman's action in declining to submit the contract was entirely appropriate.

2. Kellogg's fourth theory also focuses on the time after negotiation of the contract with Judge Hinkes. Kellogg argues that the Commission could and should have cancelled the contract and tried to negotiate another, more acceptable arrangement with Judge Hinkes. This contention was not suggested by Kellogg when it demanded that Judge Hinkes be removed from the case, and, even if it had been, it is clear from *Gamble-Skogmo, supra,* that the Commission was under no duty to pursue such a course, particularly in light of the parties' expressed desire that Judge Hinkes be removed. Moreover, such a course might well have created additional problems of its own. Had the Commission cancelled the Hinkes contract and negotiated an alternative arrangement, it would, in effect, have placed respondents, who had protested the terms of the contract, in the position of having denied Judge Hinkes the perceived benefits of the contract.

3. Kellogg's third and fifth theories are related, and center on the events leading up to the negotiation of the contract. In its third theory, Kellogg argues that the Commission illegally entered into the contract and thus deprived it of an ALJ in circumstances where other arrangements might have been possible. This theory, as we understand it, presupposes a duty on the part of the Commission to employ any legal means to retain the services of an ALJ who threatens to resign or requests special consideration as a condition of his continued service. General Mills' request for discovery and an evidentiary hearing is premised on a similar argument.[13]

In its fifth theory, Kellogg argues that, even if no such absolute duty exists, an ALJ is not unavailable where (1) he is willing and able to be rehired; (2) the agency determines that it is in the best interests of the agency to rehire the ALJ; and (3) the agency fails to use due diligence in finding a lawful means to reemploy the ALJ, all three of which conditions Kellogg claims were present here. According to Kellogg, the "duty of due diligence would consist both of

[13] A close reading of Kellogg's memorandum of April 3, 1980, suggests that Kellogg's third theory effectively partakes of two notions. On one hand, Kellogg argues that "unavailability" under Section 554(d) "does not refer to every situation where an ALJ becomes unable to serve, *but only to those situations* where the inability occurs for reasons beyond the agency control" (Kellogg Memorandum of April 3, 1980, at 16). This theory appears also to underlie the request of General Mills for discovery and an evidentiary hearing. General Mills Request at 3. If an ALJ were "available" so long as his continued service was under the Commission's control, it would follow that the Commission would be under a duty to employ any lawful means possible to retain the ALJ. Alternatively Kellogg argues that "the concept of unavailability does not encompass situations where an ALJ's inability to continue presiding * * * is unlawfully caused by the agency which employs him." Kellogg Memorandum of April 3, 1980, at 15. This assertion seems to rely on a different theory—that the agency must refrain from engaging in unlawful conduct in removing an ALJ from a case. Again, General Mills would also appear to rely on this premise. General Mills Request at 3.

identifying and pursuing a lawful arrangement and of ensuring that the individual terms of the contract formalizing that arrangement were all proper and legal" (Kellogg Memorandum of April 3, 1980, at 43). Kellogg contends that the basis of the duty is to be inferred from a variety of sources, see *id.* at 33 n.7, but cites no specific authority that articulates the duty.

It is in connection with these third and fifth theories that analysis of the factual record is appropriate.

The Commission has carefully reviewed the affidavits of Judges Hanscom and Barnes and Mr. Kefauver, and Judge Hinkes' statement, as well as the statements of Chairman Pertschuk. While, not surprisingly, the recollections of the witnesses differ in some respects, they are in accord with respect to the material facts. According to Judge Hinkes, he approached Judge Barnes in August 1978 and advised Judge Barnes that he had decided to retire, because, for personal reasons, he wanted to move to California; he was also motivated by an upcoming cost of living increase for federal retirees. Hinkes Statement at 11, 13, 29. According to Judge Hinkes, Judge Barnes then inquired how Judge Hinkes might be persuaded to remain on the case, and proposed a contract arrangement. *Id.* at 14, 29. Judge Hinkes recalled that he would not have been willing to remain in Washington to finish the case as either a regular ALJ or a reemployed annuitant. *Id.* at 12–13, 19. Judge Hinkes also suggests that he would have been willing to complete the case without a contract if the Commission had been willing (and able) to pay his moving expenses to California. *Id.* at 23, 30–35. Judge Hinkes states that this alternative was communicated to Judge Hanscom and Mr. Kefauver, but that Mr. Kefauver told him it could not be done. *Id.* at 30, 32. This testimony is generally consistent with the affidavits of Judges Hanscom and Barnes and Mr. Kefauver, except that Judge Barnes reports that Judge Hinkes stated somewhat different personal reasons for retiring; neither Judge Hanscom nor Judge Barnes report Judge Hinkes' expression of a willingness to continue as a regular ALJ if he were moved to California.

Thus, there is no dispute that in August 1978 Judge Hinkes approached Judge Barnes and stated that he intended to retire by the end of August. Similarly, there is no dispute that Judge Hinkes would not have remained on the case unless, at a minimum, the Commission transferred him, at Commission expense, to California—special treatment not accorded other Commission ALJ's. Even if the Commission could have granted such treatment to Judge Hinkes,[14] we conclude that, as a matter of law, the Commission was

[14] Under the circumstances, we think it highly unlikely that the Commission could have paid Judge Hinkes'

(Continued)

under no obligation to do so, and that no such obligation arose by reason of the Commission's efforts to retain Judge Hinkes under contract.[15]

Kellogg and General Mills point to an appendix to a statement of the Attorney General which says that "only the officer who presided at the hearing (unless he is unavailable *for reasons beyond the agency's control)* is eligible to make the initial or recommended decision * * * ." Appendix to Attorney General's Statement of October 5, 1945, on the APA, appendix to S. Rep. No. 752, 79th Cong., 1st Sess. (1946) (emphasis added). Assuming this appendix provides the proper test, the Commission has not violated its requirements. Judge Hinkes made the initial determination that he would retire and not complete the case absent extraordinary treatment; and to that extent became unavailable for reasons beyond the Commission's control.

If, however, this brief phrase is deemed to suggest that an agency is bound to afford any lawful, extraordinary treatment demanded by an ALJ, it is inconsistent with the removal procedures under federal law, and basic public policy, and we believe it cannot be credited. See also *Gamble-Skogmo, Inc.* v. *FTC, supra.* Indeed, respondents have elsewhere argued that the Commission is under a duty *not* to afford an ALJ special treatment or to negotiate with an ALJ regarding the

moving expenses. The pertinent statute authorizes reimbursement of expenses where an employee is "transferred in the interest of the Government from one official station to another for permanent duty." 5 U.S.C. 5724(a)(1) (1976). The statute further provides: "When a transfer is made primarily for the convenience or benefit of an employee, including an employee in the Foreign Service of the United States, or at his request, his expenses of travel and transportation and the expenses of transporting, packing, crating, temporarily storing, draying, and unpacking of household goods and personal effects may not be allowed or paid from Government funds." 5 U.S.C. 5724(h). Finally, the statute permits payment of moving expenses only upon the employee's written agreement to continue in government employment for 12 months after his transfer. 5 U.S.C. 5724(i).

[15] Kellogg has objected to Commissioner Clanton's presiding at the taking of Judge Hinkes' statement. Kellogg's first objection—that the APA and the Commission's rules do not permit "bifurcation" of the proceeding—has been adequately answered in Part II B, *supra.* Kellogg's second objection—that the entire Commission should have presided over the proceeding to take Judge Hinkes' statement—is equally without merit. There is to be no "initial decison" as to the proceeding regarding the circumstances of Judge Hinkes' retirement, and therefore 5 U.S.C. 554(d) & 557(b) and Section 3.51(c) of the Commission's Rules are inapplicable.

Moreover, Kellogg's argument misconceives the limited nature of the proceeding to obtain Judge Hinkes' statement. The proceeding was not an "evidentiary hearing," but an alternative to the affidavits submitted by Judges Hanscom and Barnes and Mr. Kefauver, and Commissioner Clanton's role was merely to preside over the reception of Judge Hinkes' statement. Commissioner Clanton's active participation was limited to a few, minor questions seeking clarification of points made by Judge Hinkes. The procedure adopted by the Commission in this case—calling for affidavits or statements from knowledgeable witnesses addressing the material circumstances before determining whether to afford discovery and an evidentiary hearing—is fully supported by the case law. See, *e.g., Grolier, Inc.* v. *FTC,* 615 F.2d 1215 (9th Cir. 1980); *Au Yi Lau* v. *INS,* 555 F.2d 1036, 1043 (D.C. Cir 1977); *Adolph Coors Co.* v. *FTC* 497 F.2d 1178, 1189 (10th Cir. 1974), *cert. denied,* 419 U.S. 1105 (1975); *R. A. Holman & Co.* v. *SEC,* 366 F.2d 446, 453–54 (2d Cir. 1966), *cert. denied,* 389 U.S. 991 (1967). Although respondents have pointed to a variety of alleged inadequacies or inconsistencies in the statements and affidavits, they point to no inconsistency with respect to what we have found to be the material facts bearing upon the unavailability issue. *Cf.* Fed. R. Civ. P. 56. Accordingly, we find it unnecessary to permit further discovery or to hold an evidentiary hearing on the question of Judge Hinkes' unavailability. And, because we have determined that further factual inquiry related to the unavailability issue is unnecessary, we find no need to consider under what circumstances appointment of an ALJ from outside the Commission to supervise discovery and an evidentiary hearing would be warranted.

336-345 O - 81 - 8

terms of his continued service. Kellogg Memorandum of October 10, 1978, at 20–21; General Mills Memorandum of November 29, 1978 at 7.

There is no present need to define the outer limits of the Commission's discretion to accommodate special requests of an ALJ—it is enough for the present that the Commission is under no *duty* to make such an accommodation.[16] In this case, had the Commission chosen to let Judge Hinkes retire, the parties would have no cause to complain. Instead, the Commission entered into the contract. Had the respondents consented to the arrangement, there can be no question that any objection would be waived. *United States* v. *L.A. Tucker Truck Lines,* 344 U.S. 33 (1952). Similarly, when the parties objected to the contractual arrangement, petitioned for Judge Hinkes' removal, and raised substantial arguments against the validity of the arrangement, Chairman Pertschuk properly decided not to proceed with the arrangement. By acting in a manner that the parties themselves perceived to be in their own best interests, the Commission left the parties in the same position that they would have been in had the Commission taken no action at all to keep Judge Hinkes in the case. Therefore, we conclude that the Chairman's attempt to retain Judge Hinkes did not impose on the Commission any obligation to retain Judge Hinkes that would not have been imposed in the absence of such an attempt.[17]

Accordingly, Kellogg's motion for reconsideration is denied, the December 8, 1978, order is reaffirmed, and General Mills' request for discovery is denied.

B. We turn now to the motion by General Foods to dismiss the complaint, in which the other respondents have joined. General

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[16] Counsel for Kellogg apparently has acknowledged the absence of such a duty in another case:

MR. FURTH: Well, Your Honor, I guess whether or not [the ALJ] was or wasn't rehired is a matter totally within the discretion of the FTC anyway. I think the law is probably such that the FTC cannot [*sic*] rehire anybody they don't want to rehire in the middle of a case.

Grolier, Inc., Dkt. 8879, Tr. 8467 (Feb. 10, 1975), attached as Exhibit A to Affidavit of Michael P. Lehmann in Support of Motion of Respondent Kellogg Company to Admit Certain Documents in Evidence in the Proceedings to Supplement the Record Concerning the Hinkes Matter, filed May 20, 1980. The Commission has reviewed the materials attached to the Lehmann Affidavit, and having concluded that they are immaterial to the issues herein, denies Kellogg's request that they be admitted into evidence. For the same reason, Kellogg's request, filed July 2, 1980, to admit into evidence a copy of a statement of Marvin H. Morse, Director of the Office of Administrative Law Judges, is denied. Mr. Morse's statement has no evidentiary value for purposes of this proceeding; and although it might be cited as a secondary authority on the legality of the contract with Judge Hinkes, the Commission has found it unnecessary to resolve that question.

[17] This case is readily distinguishable on its facts from *Chicago Automobile Trade Ass'n* v. *Madden,* 219 F. Supp. 828, 831 (N.D. Ill. 1963), *rev'd,* 328 F.2d 76 (7th Cir.), *cert. denied,* 377 U.S. 979 (1964), where the district court found that the examiner, who had withdrawn from the particular proceeding for health reasons, had subsequently participated in other proceedings and therefore was still available to the Board. The court also concluded that the Board was motivated, in part, "by its fear of his unfavorable decision were he permitted to resume the case." *Id.* No similar concern motivated the Commission in this case, and none is charged.

Foods contends that the Commission has deprived it of due process of law in the following respects:

A. By circumventing the procedures established by Congress for the protection of respondents' rights and deciding instead to conduct *ex parte* negotiations with a sitting judge which led to a contract arrangement which was and should have been known to be illegal;

B. By impermissibly intermingling its prosecutorial, administrative and judicial functions to the point where the prosecution formulated the course which the Commission then followed; and

C. By inducing Judge Hinkes to retire by the offer of an illegal contract, so that through its own improper actions the Commission rendered Judge Hinkes disqualified from continuing to preside in this matter.

Except for the relief requested—dismissal—General Foods' first argument does not differ substantially from the contentions of Kellogg and General Mills discussed above. The Commission rejects General Foods' contention that the efforts to retain Judge Hinkes create an appearance of impropriety which requires dismissal. As discussed above, Chairman Pertschuk has explained that his decision to seek to retain Judge Hinkes was based upon his conclusion that retention of the judge who had heard so much of the case would benefit all parties. This administrative decision was reasonable at the time, but when respondents (and complaint counsel) raised serious objections to the plan, the Chairman properly decided not to pursue it. Under these circumstances, we perceive no appearance of impropriety which requires dismissal of the proceeding—particularly in view of the important public interest in resolving the charges set forth in the complaint.

General Foods' third objection—charging that the Commission "induced" Judge Hinkes to retire—is simply unsupported by the record evidence. Judge Hinkes' statement makes it clear that he unilaterally decided to retire for personal reasons, and that only extraordinary treatment would have persuaded him to complete the case. (See pp. 17-18, *supra*.)

However, General Foods' second objection raises an issue not heretofore presented: whether the action of Judge Hanscom, a former official of the Bureau of Competition who recommended issuance of the complaint, in recommending the contract, and the participation by officials of the Bureau of Competition in meetings with Barry Kefauver, the Contracting Officer, amounted to impermissible commingling of functions under Section 554(d) and under Commission's Rule 4.7, or were otherwise unlawful under the several

theories outlined in pages 41–46 of General Foods' supporting memorandum.

Although the decision to attempt to retain Judge Hinkes was a managerial decision outside the scope of the Commission's adjudicative rules, the Commission has determined to continue the limited inquiry described below to shed additional light on the negotiating process and the role of Bureau of Competition officials in it. Accordingly, the Commission will defer, for now, ruling on the second ground of General Foods' motion.[18] The Commission has determined that the most orderly manner of proceeding is first to obtain affidavits or their equivalents from those who, from the current record, appear best able to provide the relevant facts.[19]

Conclusion

With the exception of the issues raised by General Foods as to which the Commission is undertaking further inquiry, this order is intended to dispose of all matters raised by respondents in connection with the retirement of Judge Hinkes; the parties are, of course, free to raise these issues again on appeal, if any, of Judge Berman's initial decision.

It is therefore ordered, That:

A. Kellogg's motion to disqualify Judge Berman is denied;

B. (1) The Secretary shall note for the record that the Commissioners participating in the Commission decision on this order have reconsidered the Commission's order of December 8, 1978,[20]

(2) the Commission's December 8, 1978, order is reaffirmed;

(3) Kellogg's motions of July 23, 1979 (as supplemented by its memorandum of April 3, 1980), and July 21, 1980, insofar as Kellogg seeks a trial *de novo,* an evidentiary hearing, or discovery, are denied.

C. General Mills' motion for discovery or for an evidentiary hearing is denied;

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[18] The Commission intimates no view as to the legal sufficiency of the several theories in support of dismissal advanced by General Foods in this portion of its motion.

[19] Judge Hanscom has already filed an affidavit discussing his role in the events leading to the contract with Judge Hinkes. He was not present at any meeting with Bureau of Competition officials. The Commission therefore believes that there is no present need for additional inquiry of him. General Foods' contentions concerning his role will be addressed upon the Commission's disposition of the reserved portion of its motion after the record is augmented in the manner specified.

[20] Complaint counsel's request for an extension of time, filed July 24, 1980, is denied insofar as it seeks an extension of time to address Kellogg's July 21, 1980, motion to have the Commission reconsider its order of December 8, 1978; and is granted insofar as it seeks an extension to address Kellogg's motion to disqualify Chairman Pertschuk.

D. General Foods motion to dismiss the complaint is denied except as outlined in paragraph E, *infra;*

E. (1) Barry R. Rubin and John F. Dugan shall file with the Commission, within 20 days, affidavits which set forth in detail their recollection as to the matters specified in paragraph F, *infra;* (2) Barry Kefauver shall file with the Commission, within 20 days, an affidavit which sets forth in detail his recollection as to the matters specified in paragraph F, to the extent that he has not addressed these matters in his affidavit of December 13, 1979; (3) the Secretary shall send to Daniel C. Schwartz and Peter Brickfield the attached letters, requesting them to file with the Commission, within 20 days, affidavits which set forth in detail their recollection as to the matters specified in paragraph F; and (4) the Secretary shall simultaneously place on the docket of this proceeding, and serve upon the parties, these affidavits at such time as all of them have been received. The Commission shall, upon review of the affidavits, determine what further inquiry, if any, is necessary; and

F. The affidavits required by paragraph E shall address the following:

(1) the circumstances under which each affiant first learned that Judge Hinkes was contemplating retirement;

(2) the time, place, and substance of any conversation prior to September 8, 1978, with persons outside the Bureau or office in which the affiant was employed concerning Judge Hinkes' retirement, retention under contract, or other status;

(3) the identity of all persons with whom such conversations took place;

(4) the time, place, and substance of any conversation concerning arrangements for a meeting held on August 14, 1978 at which Messrs. Schwartz, Dugan, Kefauver, Brickfield and Rubin attended, according to the Kefauver affidavit of December 13, 1979;

(5) the substance of discussion at that meeting, and in particular, whether any participant at the meeting discussed rulings that Judge Hinkes had made or might make in Docket No. 8883;

(6) the time, place, and substance of any conversation concerning arrangements for a meeting held on August 16, 1978, at which Messrs. Schwartz, Dugan, and Kefauver attended, according to the Kefauver affidavit of December 13, 1979; and

(7) the substance of discussion at that meeting, and in particular, whether any participant at the meeting discussed rulings that Judge Hinkes had made or might make in Dkt. 8883.

G. The authority of the ALJ to issue his order of May 14, 1980, is

affirmed, and the ALJ's request for an extension of time for filing the initial decision is granted.

H. Kellogg's requests to admit certain documents in evidence, filed May 20, 1980, and July 2, 1980, are denied.

I. Kellogg's objections to having Commissioner Clanton preside at the taking of Judge Hinkes' statement are overruled.

Chairman Pertschuk and Commissioner Pitofsky did not participate.

IN THE MATTER OF

BILL CROUCH FOREIGN, INC., d/b/a BILL CROUCH IMPORTS, INC. (formerly MAZDA OF BOULDER, INC.)

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-3030. Complaint, July 31, 1980—Decision, July 31, 1980

This consent order requires, among other things, a Boulder, Colo. retail dealer for new Honda automobiles to cease from charging customers more than its actual cost for transporting vehicles to its showroom; misrepresenting that optional equipment is installed by the manufacturer or required by law; and failing to disclose to customers any additional charges that would be included in the purchase price of the automobile. The order further requires the firm to make refunds, in a prescribed manner, to eligible Honda Accord customers who had paid more than $30.00 above the actual cost for freight; and retain specified records for a period of two years.

Appearances

For the Commission: *John H. Evans* and *Allen R. Franck*

For the respondent: *Miles C. Cortez, Jr.* and *Debra R. Lappin, Welborn, Dufford, Cook & Brown,* Denver, Colo.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act (15 U.S.C. 41, *et seq.,* as amended), and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that Bill Crouch Foreign, Inc., dba Bill Crouch Imports, Inc. (formerly Mazda of Boulder, Inc.), a corporation, hereinafter sometimes referred to as "respondent," has violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint, stating its charges in that respect as follows:

PARAGRAPH 1. Respondent is a corporation organized, existing, and doing business under and by virtue of the laws of the State of Colorado with its principal office and principal place of business located at 2555 Thirtieth St., Boulder, Colorado.

PAR. 2. Respondent is now, and for some time has been, engaged in the advertising, offering for sale, and sale of new automobiles, and the parts and equipment thereof, to retail customers. Respondent is an authorized dealer for the Honda Automobile Company.

PAR. 3. Respondent's volume of business is substantial and its acts and practices, as set forth herein, are in or affect commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended.

COUNT I

The allegations contained in Paragraphs One through Three are incorporated by reference herein as if fully set forth verbatim.

PAR. 4. In the course of offering for sale and selling new Honda automobiles to retail customers, respondent regularly has listed on purchase orders and bills of sale, and has collected from customers as part of the total purchase price, a charge for "Freight." This terminology represents that the charge is intended to reimburse the respondent for its actual costs or outlays to third parties for the transportation of new automobiles to the dealership from the point where they are delivered by the manufacturer.

PAR. 5. In truth and in fact, in many instances the charges referred to in Paragraph Four, which respondent has listed and collected from customers for "Freight," have exceeded respondent's actual outlays to third parties for the transportation of new automobiles.

PAR. 6. The practices described hereinabove have had the capacity and tendency to mislead and deceive new automobile consumers and have induced customers to make payments which they might not have made but for respondent's aforesaid representations.

PAR. 7. Respondent's conduct as alleged in Count I was and is to the detriment and injury of the purchasing public and constituted, and now constitutes, unfair or deceptive acts or practices in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act. Furthermore, respondent's retention of funds collected from customers by means of such conduct constituted, and now constitutes, an unfair or deceptive act or practice in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act.

COUNT II

The allegations contained in Paragraphs One through Seven are incorporated by reference herein as if fully set forth verbatim.

PAR. 8. In the further course of selling new Honda automobiles to retail customers, respondent or respondent's agents regularly have represented to customers that the application or installation of

several dealer-installed items, including, but not limited to, "undercoating" and "Polyglycoat" (a chemical paint polish and sealant), is recommended, required, or performed by the automobile manufacturer or that the respondent has no control over the installation or application of these items.

PAR. 9. In truth and in fact, the items referred to in Paragraph Eight are installed or applied at the direction of respondent to new automobiles which come into respondent's possession. Furthermore, the manufacturer of these new automobiles neither recommends, requires, nor performs the installation or application of these items.

PAR. 10. Respondent's representations as set forth in Paragraph Eight were and are false and misleading. Relying upon such representations, customers have been misled into accepting and paying for items that they might otherwise not have purchased.

PAR. 11. Respondent's conduct as alleged in Count II was and is to the detriment and injury of the purchasing public, and constituted, and now constitutes, unfair or deceptive acts or practices in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the Denver Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act, as amended; and

The respondent and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having hereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Acts, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the

procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent Bill Crouch Foreign, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Colorado, with its office and principal place of business located at 2555 Thirtieth St., in the City of Boulder and State of Colorado.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

ORDER

For purposes of this Order:

1. "New automobile" shall mean any passenger car or station wagon the equitable or legal title to which has never been transferred by a manufacturer, distributor, or dealer to an ultimate purchaser.

2. "Optional equipment" shall mean, with respect to any new automobile, any equipment or features not included within the manufacturer's suggested retail price, as defined in 15 U.S.C. 1232(f)(1).

I

It is ordered, That respondent Bill Crouch Foreign, Inc., a corporation, its successors and assigns, and its officers, and respondent's agents, representatives and employees, directly or through any corporate or other device, in connection with any sale, offering for sale, advertising or distribution of new automobiles, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from:

1. Listing on stickers affixed to any new automobile, or on purchase orders, bills of sale, or sales contracts, and collecting from consumers, any freight, transportation or destination charges that exceed respondent's cost as determined herein for the shipment of the new automobile from any port-of-entry to respondent's showrooms. For purposes of this Order, respondent's cost shall be deemed to be the amount shown on the most recent invoice received by respondent covering the shipment of comparable automobiles from a

comparable port-of-entry to respondent's showrooms plus five dollars ($5.00).

2. Affirmatively representing that any optional equipment is recommended, required, or installed by the manufacturer or is required by law, unless such is in fact the case; *provided, however,* that this requirement shall not be construed to impose a duty on respondent or its agents to affirmatively disclose information regarding such optional equipment, including but not limited to the nature or source of or requirement for such equipment, except in response to a specific consumer inquiry.

3. Failing to disclose clearly and conspicuously, prior to signing of a completed purchase order, if the total purchase price exceeds the manufacturer's suggested retail price, the precise amount of any handling, service, or similar charges which will be included in the purchase price of a new automobile.

II

It is further ordered, That:

1. The respondent shall submit to the Commission, within fifteen (15) days after the date this Order is served on respondent's corporate president (hereinafter "date of service"), a notarized affidavit, executed by the president of respondent to the effect that the respondent has made or has caused to be made a good faith search of documents that pertain to purchasers of new Honda Accord automobiles from the respondent and that the respondent, to the best of its knowledge, has previously or simultaneously with said affidavit submitted to the Commission the names of all purchasers of such automobiles covered by this Order.

2. The respondent shall submit to the Commission, within sixty (60) days after the date of service, all necessary documents, including but not limited to, purchase orders, bills of sale, buyer's orders, freight invoices and billings, internal worksheets, and invoices and all other materials necessary for the Commission to determine the amount paid by the respondent to third parties for freight. Based upon the information supplied to the Commission by the respondent pursuant to this paragraph and Paragraph II(1), the Commission or its designee shall deliver to respondent a list of all purchasers of new Honda Accord automobiles who are "eligible class members," setting forth the amount of refund due from the respondent to each such class member, derived in accordance with Part II of this Order, which list shall be served on the respondent.

3. On the ninetieth (90th) day after service on the respondent of

the list of eligible class members as provided in Paragraph II(2) above, the respondent shall make refunds to eligible class members in the following manner:

(a) except as provided in subparagraph (b) below, submit to the Commission or its designee a refund check, undated, drawn on the account of respondent made payable to each eligible class member or his or her legal representative in the amount provided by the Commission;

(b) in the event a refund check for any eligible class member is not so submitted, submit to the Commission or its designee a list of "disputed eligible class members" stating the reasons why the purchaser whose name is shown on the list prepared by the Commission is not an eligible class member or is not entitled to the refund in the amount specified by the Commission, as the case may be. If necessary, counsel for the Commission and counsel for the respondent shall thereafter confer and determine if and/or in what amount a refund is due and owing to any such disputed eligible class member.

4. Thereafter, the Commission or its designee shall send to each eligible class member, by registered mail, with return receipt requested, and with copy to respondent, a letter in the language, manner, and form shown in Appendix A, with an enclosed stamped envelope showing the address of the Commission or its designee. Upon receipt of the executed Receipt and Waiver form from an eligible class member, as provided in Appendix A, the Commission or its designee shall thereafter enter a current date on the appropriate refund check submitted to the Commission by respondent in accordance with Paragraph II(3) above and forward the check to such eligible class member.

5. On or before the three-hundredth (300th) day after date of service, the Commission or its designee shall serve on respondent (a) a list of names, addresses and received refunds in accordance with the provisions of this Part II, and (b) a list of names, addresses and refund amounts of those eligible class members whose initial mailing in the form of Appendix A or refund check was returned by the United States Postal Service. The Federal Trade Commission shall have one year from the date of service of this list to locate such eligible class members. At such time as any class member is located, the Federal Trade Commission shall follow the procedure authorized in Paragraph II(4) above with respect to the initial mailing of a letter in the form of Appendix A and subsequent mailing, if appropriate, of a refund check to such eligible class member.

6. The respondent shall, on the three-hundred and thirtieth (330th) day after the date of service, file with the Commission a report in writing setting forth the manner and form in which it has complied with Part II of this Order.

7. At the end of the one-year period described in Paragraph II(5) above, the Commission shall return to the respondent all refund checks payable to eligible class members whom the Commission is unable to locate and respondent shall thereupon be relieved of any further obligation to make payments to such eligible class members.

8. Except as modified by Paragraph II(9) below, "eligible class members" means those persons who purchased any new Honda Accord automobile at the respondent's showrooms between July 15, 1976 and the date of service of this Order, and who paid any amount for "freight," or charge of similar import, in excess of respondent's actual outlays to third parties to transport the automobile from the port-of-entry to respondent's showrooms, if such actual outlays are known, or, if unknown, in excess of respondent's outlays as computed pursuant to subparagraph 10(b) below.

9. If at the time of sale the charge made by the respondent for "freight" to a person who purchased a new Honda Accord automobile between July 15, 1976 and the date of service of this Order was a "good faith estimate" of the respondent's actual freight outlays to third parties, such person shall not be an "eligible class member" within the meaning of this Consent Order. Any charge for freight made by the respondent shall be deemed a "good faith estimate" by the respondent if such charge cannot be shown to have exceeded the respondent's subsequent actual outlays, or, if unknown, its estimated outlays, as determined under subparagraph 10(b) below, to third parties for transportation of the automobile from the port-of-entry to the respondent's showrooms by more than thirty dollars ($30.00).

10. The respondent shall make refund payments to each eligible class member as follows:

(a) each eligible class member shall receive as a refund one-half (1/2) of that amount by which the charge paid by the class member to the respondent for "freight" exceeded the respondent's actual outlays to third parties for transportation of the automobile purchased by the class member from the port-of-entry to respondent's showrooms.

(b) if such actual outlay is unknown, each eligible class member shall receive as a refund one-half (1/2) of that amount by which the charge paid by the class member to the respondent for "freight" exceeded the average sum paid by the respondent to third parties to

transport automobiles comparable to that purchased by the class member from comparable ports-of-entry to respondent's showrooms during the three (3) calendar months preceding the month of sale to the class member.

The amount of each refund under this section shall be determined by the Commission on the basis of the information supplied by the respondent under Paragraph II(2) above.

11. The respondent shall maintain records and documents for two (2) years after the filing of the report referred to in Paragraph 6 of Part II of this Order, which demonstrate that the respondent has complied with Part II of this order.

12. If any duty required to be performed on a certain day under Part II of this Order falls upon a non-business day, the respondent herein shall perform such duty on the next following business day.

III

It is further ordered, That:

1. Respondent shall notify the Commission at least thirty (30) days prior to any proposed changes in the corporate respondent such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries, or any other changes in the corporation which may affect compliance obligations arising out of the Order.

2. Respondent shall forthwith deliver a copy of this Order to each of its operating divisions and to each of its present and future officers; and forthwith deliver a summary of this Order, stating that the respondent is subject to an order of the Commission and enumerating the requirements of Part I of this order, to each employee or agent who is engaged in the sale of new automobiles, or who, directly or indirectly, has any responsibility relating in any way to the pricing of new automobiles, or who is engaged in any aspect of the preparation, creation, or placing of advertising; and the respondent shall secure a signed statement acknowledging receipt of said order or summary from each such person.

3. Respondent shall retain each of its sales contracts and freight invoices for new automobiles for two (2) years after the date of the sales transaction, and shall make such records available for inspection and copying upon reasonable request by the Commission or any of its duly authorized representatives.

4. Respondent shall, at reasonable times, afford the Commission, or any of its duly authorized representatives, access to such records,

memoranda, and other documents relating to the provisions contained herein as may be appropriate to enable the Commission to determine respondent's compliance with the Order.

5. Respondent shall within sixty (60) days after service of this Order upon respondent file with the Commission a report, in writing, setting forth in detail the manner and form in which it has complied with this Order.

IN THE MATTER OF

BENEFICIAL CORPORATION, ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-3032. Complaint, August 5, 1980—Decision, August 5, 1980

This consent order requires, among other things, a Wilmington, Del. firm and Beneficial Management Corp. of Morristown, N.J. to cease, in connection with the extension of consumer credit and purchase of consumer contracts, from misrepresenting the effect of state laws and consumer's right to assert against contract holder any claim or defense arising from the contract. The order further bars respondents from using past notice to defeat any valid consumer claim and requires them to notify all active account consumers who received the notice that their claims and defenses have not been waived.

Appearances

For the Commission: *Ivan L. Orton* and *Randall H. Brook.*

For the respondents: *John P. Howland,* for Beneficial Management Corporation, Morristown, N.J.

COMPLAINT

The Federal Trade Commission, having reason to believe that Beneficial Corporation and Beneficial Management Corporation have violated Section 5 of the Federal Trade Commission Act, as amended, and that a proceeding is in the public interest, issues this complaint.

PARAGRAPH 1. Respondent Beneficial Corporation ("Beneficial") is a Delaware corporation with its office and principal place of business at 1300 Market St., Wilmington, Delaware.

Respondent Beneficial Management Corporation ("Beneficial Management") is a Delaware corporation with its office and principal place of business at 200 South St., Morristown, New Jersey.

Beneficial directs and controls the Beneficial Finance System comprised of wholly owned subsidiaries including local loan offices and Beneficial Management. Beneficial Management provides centralized accounting, auditing and legal services to these consumer finance subsidiaries.

Allegations below stated in the present tense include the past tense.

PAR. 2. Beneficial through Beneficial Finance System is engaged in the extension of consumer credit to the general public. It purchases

installment contracts and other consumer credit agreements from retailers in addition to making direct consumer loans.

PAR. 3. In connection with the extension of consumer credit and purchase of contracts, Beneficial and Beneficial Management has supervised the dissemination of legal forms and other printed materials throughout the country. This is done through the United States mails. Beneficial and Beneficial Management maintain a substantial course of trade in extending consumer credit and purchasing retail contracts in or affecting commerce as "commerce" is defined in the Federal Trade Commission Act, as amended.

PAR. 4. In the course of purchasing consumer credit contracts, the Beneficial Finance System becomes a holder of these consumer credit contracts as "holder" is used in the FTC Trade Regulation Rule, Preservation of Consumer Claims and Defenses, 16 C.F.R. 433 (the "Holder Rule").

PAR. 5. These contracts usually, if not always, contain the following notice as required by the Holder Rule.

ANY HOLDER OF THIS CONSUMER CREDIT CONTRACT IS SUBJECT TO ALL CLAIMS AND DEFENSES WHICH THE DEBTOR COULD ASSERT AGAINST THE SELLER OF GOODS OR SERVICES OBTAINED PURSUANT HERETO OR WITH THE PROCEEDS HEREOF. RECOVERY HEREUNDER BY THE DEBTOR SHALL NOT EXCEED AMOUNTS PAID BY THE DEBTOR HEREUNDER.

This notice is required by the FTC to preserve the consumer's legally sufficient claims and defenses so that they may be asserted against a creditor where a seller fails to keep its side of the bargain.

PAR. 6. Upon purchasing these contracts, the Beneficial Finance System sends "Notification of Purchase" forms to the consumers whose contracts were purchased. These notices contain the following language or language to the following effect:

THE FOLLOWING REFERENCES MAY APPLY TO THE STATE(S) INDICATED

ARIZONA—YOU HAVE NINETY (90) DAYS FROM THE DATE OF RECEIPT OF THE GOODS OR RENDERING OF SERVICES WITHIN WHICH TO NOTIFY US IN WRITING OF ANY COMPLAINTS, CLAIMS OR DEFENSES WHICH YOU MAY HAVE AGAINST THE SELLER. SUCH WRITTEN NOTICE MUST BE SENT BY CERTIFIED MAIL TO THE SELLER AND YOU SHOULD FORWARD A COPY TO US. IF SUCH WRITTEN NOTICE IS NOT RECEIVED WITHIN THE NINETY (90) DAY PERIOD, THE ASSIGNEE WILL HAVE THE RIGHT TO ENFORCE THE CONTRACT FREE OF ANY CLAIMS OR DEFENSE THE BUYER OR LESSEE MAY HAVE AGAINST THE SELLER OR LESSOR WHICH HAS ARISEN BEFORE THE END OF THE NINETY (90) DAY PERIOD.

DELAWARE—WITHIN 15 DAYS OF THE DATE OF MAILING OF THIS NOTICE YOU MUST NOTIFY THIS OFFICE IN WRITING OF ANY FACTS GIVING RISE TO ANY CLAIM OR DEFENSE THAT YOU MAY HAVE AGAINST THE SELLER OR ELSE SUCH CLAIM IS WAIVED.

IDAHO—. . . THREE (3) MONTHS . . .

INDIANA AND SOUTH DAKOTA—. . . 60 DAYS . . .

IOWA, NORTH CAROLINA, OKLAHOMA AND TENNESSEE—. . . 30 DAYS . . .

MARYLAND—. . . NINETY (90) DAYS . . .

PENNSYLVANIA AND WYOMING—. . . 45 DAYS . . .

TEXAS—. . . 3 DAYS . . .

WEST VIRGINIA—. . . 180 DAYS . . .

WISCONSIN—. . . 12 MONTHS . . .

PAR. 7. The representation that the consumer waives the right to assert claims or defenses if the Beneficial Finance System is not notified is false. Consumers continue to have this right as stated in the contract.

State laws like those referenced by the Beneficial Finance System on the "Notification of Purchase" forms might apply to contracts not governed by the Holder Rule. However, some of the references themselves misrepresent state law. All of the references misrepresent the impact of state law on contracts governed by the Holder Rule.

PAR. 8. The notice has the tendency and capacity to deter consumers from asserting valid claims and defenses against the Beneficial Finance System.

For example, consumers with valid warranty claims against a seller might feel that they had no claim against the Beneficial Finance System and had to continue making payments. This would undermine the purpose of the Holder Rule.

PAR. 9. For the reasons stated above, the acts and practices of Beneficial and Beneficial Management are to the prejudice and injury of the public and constitute false, misleading, deceptive and unfair acts or practices in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act, as amended.

DECISION AND ORDER

The Federal Trade Commission has initiated an investigation of certain acts and practices of the respondents Beneficial Corporation and Beneficial Management Corporation. The respondents have been furnished with a copy of a draft of complaint which the Seattle Regional Office proposed to present to the Commission for its consideration. This complaint, if issued by the Commission, would charge respondents with violation of the Federal Trade Commission Act, as amended.

The respondents, their attorney, and counsel for the Commission have executed an agreement containing a consent order, an admission by the respondents of all the jurisdictional facts set forth in the draft complaint, a statement that the signing of the agreement is for settlement purposes only and does not constitute an admission by respondents that the law has been violated as alleged in the complaint, and waivers and other provisions as required by the Commission's Rules.

The Commission considered the matter and determined that it had reason to believe that the respondents have violated the Federal Trade Commission Act, as amended, and that complaint should issue. It then accepted the executed consent agreement and placed it on the public record for a period of 60 days. Part III of the Order has been modified to follow the complaint allegations. The correction notice required by Part III must be sent only to accounts in the 15 states whose laws were misrepresented by Beneficial's original notice. Now, in conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission issues its complaint, makes the following jurisdictional findings and enters the following Order:

1. Respondent Beneficial Corporation is a Delaware corporation. Its office and principal place of business is located at 1300 Market St., Wilmington, Delaware.

Respondent Beneficial Management Corporation is a Delaware corporation. Its office and principal place of business is located at 200 South St., Morristown, New Jersey.

Respondent Beneficial Corporation directs and controls the Beneficial Finance System comprised of wholly-owned subsidiaries including local loan offices and Beneficial Management.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents.

3. The proceeding is in the public interest.

Order

This order applies to respondents Beneficial Corporation ("Beneficial") and Beneficial Management Corporation ("Beneficial Management"), their successors, assigns, officers, agents and employees, whether acting directly or through any corporation, subsidiary, division or other device, including any part of the Beneficial Finance System.

I.

It is ordered, That Beneficial and Beneficial Management cease

and desist from representing, directly or by implication, that a consumer's right to assert claims or defenses against a holder of the consumer's contract:

A. is contingent upon the consumer giving notice of the claim or defense to the holder within a stated time after the holder purchases the contract;

B. is in any other way limited by state law unless this is true.

II.

It is further ordered, That Beneficial not assert any defect in a consumer's assertion of a claim or defense against the Beneficial Finance System (or any part of it) when that defect is based on the consumer's failure to give prior notice to the Beneficial Finance System (or any part of it).

III.

It is further ordered, That Beneficial Management, within 30 days after service of this order, send the following notice to all active installment sales contract accounts in Arizona, Delaware, Idaho, Indiana, Iowa, Maryland, North Carolina, Oklahoma, Pennsylvania, South Dakota, Tennessee, Texas, West Virginia, Wisconsin and Wyoming:

Dear Customer:

When we purchased your contract, we sent you a notice. This notice said you might not have the right to assert claims or defenses against us unless you notified us within a certain time period.

This statement was not correct.

You have always had the right to assert claims or defenses against us that you could assert against the seller. You have this right even if you have not previously told us of your claim or defense.

Beneficial Finance System
Affiliated Companies

IV.

It is further ordered, That respondents maintain complete business records relative to the manner and form of their compliance with this Order. Respondents shall retain each record for at least three years. Upon reasonable notice, respondents shall make any and all

the records available for inspection and photocopying by authorized representatives of the Federal Trade Commission.

V.

It is further ordered, That Beneficial forthwith distribute a copy of this Order to each office of its respective domestic consumer finance subsidiaries.

VI.

It is further ordered, That respondents notify the Commission at least 30 days prior to any proposed change in a corporate respondent in which the respondent is not a surviving entity, such as dissolution, assignment or sale resulting in the emergence of any successor corporation or corporations, or any other change in the corporation which may affect compliance obligations arising out of the Order.

VII.

It is further ordered, That respondents shall, within 60 days after service of this Order, file with the Commission a report setting forth in detail the manner and form in which they have complied with this Order.

IN THE MATTER OF

HERBERT R. GIBSON, SR., ET AL.

MODIFYING ORDER AND OPINION IN REGARD TO ALLEGED VIOLATION OF SEC. 2 OF THE CLAYTON ACT AND THE FEDERAL TRADE COMMISSION ACT

Docket 9016. Final Order, April 30, 1980—Modifying Order, Aug. 8, 1980

This order, granting in part, and denying in part, respondents' petitions for reconsideration, modifies the order issued on April 30, 1980, 45 FR 38352, 95 F.T.C. 564, by inserting the word "while" before the word "acting," in paragraph 1, line 2 of Section II; and by inserting a comma and the phrase "while acting as a buyer or acting for in behalf of or subject to the direct or indirect control of a buyer," after the word "respondent[s]," in paragraph 2, line 3 of Section II.

ORDER GRANTING IN PART, AND DENYING IN PART, RESPONDENTS' PETITIONS FOR RECONSIDERATION

An opinion and final order in this matter having been issued on April 30, 1980; respondents having been served by mail with the said opinion and order on May 20, 1980 and May 21, 1980; respondents having petitioned for reconsideration of said opinion and order on June 12, 1980; and the Commission, for the reasons stated in the accompanying opinion, having determined to grant in part, and deny in part, respondents' petitions for reconsideration;

It is ordered, That the final order to cease and desist be, and hereby is, modified as follows:

In paragraph 1 of Section II of the Order, line 2, insert the word "while" in front of the word "acting"; and

In paragraph 2 of Section II of the Order, line 3, after the word "respondent[s]," insert a comma and the phrase "while acting as a buyer or acting for or in behalf of or subject to the direct or indirect control of a buyer,".

OPINION OF THE COMMISSION

BY CLANTON, *Commissioner:*

Respondents have filed two petitions for reconsideration of our recent opinion and order. Each petition asserts: (1) that the language and coverage of Section II of the Final Order should be changed; (2) that application of the opinion of the Court of Appeals in *Grolier, Inc.* v. *FTC,* 615 F.2d 1215 (9th Cir. 1980), requires disqualification of the administrative law judge ("ALJ"), Theodor P. von Brand, and hence

dismissal or remand of the case; and (3) that certain actions taken by the Commission during periods of allegedly lapsed appropriations, including actions taken in the investigation and adjudication of this case, violated the Antideficiency Act, 31 U.S.C. 665(a) (1976), and hence require dismissal or remand of the case.

Section 3.55 of the Commission's Rules of Practice limits the scope of a petition for reconsideration to "new questions raised by the decision or final order and upon which the petitioner had no opportunity to argue before the Commission." While certain of respondents' objections are appropriate for disposition by reconsideration, other contentions are not new or are untimely. We consider each of the objections raised *seriatim.*

A.

The petition filed by Herbert R. Gibson, Jr., Gerald P. Gibson and others objects to the inclusion of any respondent other than Herbert R. Gibson, Sr. in the provisions of Section II of the Final Order, which essentially enjoins respondents from violating Section 2(c) of the Clayton Act, 15 U.S.C. 13(c) (1976), as amended. This issue of order coverage is not new and these respondents had ample opportunity, which they exercised, to address this question during the course of trial and on appeal to the Commission. See, *e.g.,* Answering Brief of Herbert R. Gibson, Jr., filed May 29, 1979, at 9. The instant request is, therefore, inappropriate, *cf. Interstate Builders, Inc.,* 72 F.T.C. 1009, 1010 (1967); *Lester S. Cotherman,* 77 F.T.C. 1621, 1622 (1970), and is denied.

The petition filed by Herbert R. Gibson, Sr. and Belva Gibson notes that the language of paragraphs 1 and 2 of Section II of the Final Order are at variance, in that only the former includes the phrase "as a buyer or acting for or in behalf of or subject to the direct or indirect control of a buyer." The petition requests that the latter paragraph be altered to conform to the former. As the petitioners surmise, it was the Commission's intention that this phrase appear in both paragraphs, and an appropriate order correcting this typographical omission is annexed. To sum up, all Gibson respondents, except dissolved corporations, are bound by Section II of the Final Order not to receive or induce payments which would violate Section 2(c) of the Clayton Act. This proscription applies irrespective of whether the respondent acts as a buyer, or on behalf of or subject to the control of a buyer.

B.

All respondents petition for reconsideration of the Commission's opinion and order in light of *Grolier, Inc.* v. *FTC,* 615 F.2d 1215 (9th Cir. 1980). In that case, the Commission issued a complaint charging Grolier with violating Section 5 of the Federal Trade Commission Act. During the course of the hearings, Administrative Law Judge von Brand advised the parties that he had previously served as an attorney-advisor to former Commissioner Everette MacIntyre from 1963 to January 1971, during which time the Commission was investigating Grolier and its subsidiaries. "Upon learning of ALJ von Brand's advisory responsibility during the eight-year period, Grolier requested that the judge disqualify himself from further participation in the proceedings." 615 F.2d at 1217. Judge von Brand declined to recuse himself, and the Commission affirmed Judge von Brand's decision in an interlocutory order, 87 F.T.C. 179, 179–81 (1976), and again in its final order and opinion, 91 F.T.C. 315, 485–86 (1978). On appeal, the Ninth Circuit concluded that the Commission had incorrectly interpreted Section 5(c) of the Administrative Procedure Act, 5 U.S.C. 554(d) (1976), in ruling on Grolier's disqualification challenge, and remanded the case to the Commission.

Although respondents in this case have not submitted a motion and affidavits as required by Rules of Practice Section 3.42(g)(2),[1] we understand the facts to be essentially as follows. Beginning in 1967, the Commission and its staff investigated respondents; the investigation culminated in a complaint issued in 1975. Judge von Brand presided over the proceedings from the issuance of the complaint, through trial (which began on December 19, 1977), and until his issuance of the initial decision in early 1979.

Judge von Brand had previously served with the Commission as an attorney-advisor to Commissioner MacIntyre from 1963 until 1971. During Judge von Brand's tenure as attorney-advisor to Commissioner MacIntyre, the Commissioners themselves, including Commissioner MacIntyre, participated in certain decisions connected

[1] In relevant part, Rules of Practice Section 3.42(g), 16 C.F.R. 3.42(g), provides: "Whenever any party shall deem the Administrative Law Judge for any reason to be disqualified to preside, or to continue to preside, in a particular proceeding, such party may file with the Secretary, a motion addressed to the Administrative Law Judge * * * to be supported by affidavits setting forth the alleged grounds for disqualification." The requirement of affidavits, grounded in 5 U.S.C.556 (1976), is not an empty formality to be cast aside unilaterally by a party to a Commission proceeding. There are many reasons for such a requirement. An affidavit provides an exact, sworn recitation of facts, collected in one place; a disqualification motion must not be made by a party, nor taken by the Commission, lightly. "Such a charge, unfairly made, not only impugns without warrant the integrity of the government official entrusted with responsibility for deciding a given dispute, but it also unnecessarily tarnishes our beneficent traditions of legal due process." *Marcus* v. *Director, Office of Wkrs' Comp. Prog.,* 548 F.2d 1044, 1050 (D.C. Cir. 1976) (per curiam). Accordingly, the affidavit requirement serves not only to focus the facts underlying the charge, but to foster an atmosphere of solemnity commensurate with the gravity of the claim. Respondents' failure to submit affidavits is thus an independently sufficient basis to deny their petitions in this respect.

with the investigation of respondents (*e.g.*, the Commission voted on two investigational resolutions and ruled on a motion to quash three subpoenas).

In a pretrial conference on February 23, 1977 (about one year after issuance of the Commission's interlocutory opinion affirming Judge von Brand's participation in *Grolier, supra,* and almost ten months before the start of trial in this case), Judge von Brand, apparently acting out of candor and an abundance of caution, disclosed to the parties on the record[2] the fact of his prior service to Commissioner MacIntyre, and recited his "understanding that none of the respondents * * * would raise an objection to [his] continuing in the case on that ground." (Tr. at 242.) All counsel, including counsel for the instant petitioners, responded unequivocally that there would be no such objection. (*Id.* at 242–43.) The case proceeded through trial, and, consistent with their statements, respondents did not object to Judge von Brand's participation. Neither did respondents object in their appeal papers before the Commission, or at oral argument in July, 1979.

The Ninth Circuit's opinion in *Grolier* was issued on January 24, 1980; respondents did not attempt to present a *Grolier*-type challenge to Judge von Brand in this case before the Commission's decision and order issued on April 30, 1980.

Respondents now urge, for the first time, that the Ninth Circuit's decision in *Grolier* requires the Commission, under the Constitution, the Administrative Procedure Act, and the Commission's Rules of Practice[3] either (1) to disqualify Judge von Brand and (a) dismiss the case or (b) vacate its decision and remand for a new trial;[4] or (2) to grant discovery in the form, *inter alia,* of a deposition from Judge

[2] The transcript reveals that Judge von Brand disclosed his prior service off the record as well. (Tr. at 242.)

[3] The Court of Appeals' decision in *Grolier* involved only an interpretation of Section 5(c) of the Administrative Procedure Act, 5 U.S.C. 554(d) (1976), and did not purport to interpret the Constitution or the Commission's Rules of Practice; accordingly, it offers no basis for relief on those grounds.

Respondents' very general assertion of their right to trial by a "fair and impartial judiciary" is based upon the due process clause of the Fifth Amendment. While we are and must be sensitive to such considerations, neither will we substitute our judgment for that of the federal judiciary or the Congress. Assuming *arguendo* that Judge von Brand possessed some familiarity with the facts of the case gained through his service to Commissioner MacIntyre (notwithstanding that Judge von Brand's tenure as an attorney-advisor ended four years before issuance of the complaint), his presiding over the trial would not constitute a due process violation. "Mere familiarity with the facts of a case gained by an agency in the performance of its statutory role does not * * * disqualify a decisionmaker." *Hortonville Joint School District No. 1* v. *Horton Education Ass'n,* 426 U.S. 482, 493 (1976); *accord, Withrow* v. *Larkin,* 421 U.S. 35, 47–59 (1975) (contention that combination of investigative and adjudicative functions violates due process carries difficult burden of persuasion); *Pangburn* v. *CAB,* 311 F.2d 349, 358 Cir. 1962). Moreover, under the exception contained in the fourth sentence to Section 5(c) of the APA, agency members may participate in investigative and adjudicative decisions in the same case. To hold that Judge von Brand's participation violated the Constitution would thus be to declare that the Administrative Procedure Act is constitutionally deficient. *Cf. Withrow* v. *Larkin, supra,* 421 U.S. at 56 (APA not unconstitutional).

As to the respondents' reference to the Commission's Rules, they cite none, and we are aware of none, that might be relevant.

[4] Even if fully applicable, *Grolier* at most would require reconsideration by the Commission. The Ninth Circuit's opinion, by its terms, requires neither retrial nor dismissal. 615 F.2d at 1222.

von Brand and access to Commission records. In our view, even apart from estoppel due to respondents' waiver, there is an important element—timeliness—present in *Grolier,* but lacking here, which makes the cases altogether different; indeed, respondents' lack of timeliness bars them from any relief.

"A basic requirement for any disqualification motion is, of course, that it be presented either at the outset of the proceeding or immediately after ascertainment of the circumstances that prompt its filing." *Kroger Co.,* Dkt. 9102 (Order filed June 5, 1980, at 2) (quoting 5 U.S.C. 556(b)). See Rules of Practice Section 3.42(g)(2) (motion to be filed "[w]henever" a party deems ALJ disqualified; also provides for expedited Commission determination). In this respect, the Commission's requirements are consistent with the "general rule governing disqualification, normally applicable to the federal judiciary and the administrative agencies alike," that disqualification claims must be raised "as soon as practicable after a party has reasonable cause to believe that grounds for disqualification exist." *Marcus* v. *Director, Office of Wkrs.' Comp. Prog.,* 548 F.2d 1044, 1051 (D.C. Cir. 1976) (per curiam) (footnotes omitted); *accord, Capitol Transp., Inc.* v. *United States,* 612 F.2d 1312, 1325 (1st Cir. 1979); *Duffield* v. *Charleston Area Medical Center, Inc.,* 503 F.2d 512, 515–16 (4th Cir. 1974) (collecting cases); *Safeway Stores, Inc.* v. *FTC,* 366 F.2d 795, 802–03 (9th Cir. 1966), *cert. denied,* 386 U.S. 932 (1967); *R. A. Holman & Co.* v. *SEC,* 366 F.2d 446, 454–55 (2d Cir. 1966), *cert. denied,* 389 U.S. 991 (1967); *Marquette Cement Mfg. Co.* v. *FTC,* 147 F.2d 589, 592 (7th Cir.), *aff'd,* 333 U.S. 683 (1945). See also *United States* v. *L. A. Tucker Truck Lines,* 344 U.S. 33, 38 (1952). The rule of timeliness requires that a party act as soon as possible after the facts have become known. *Satterfield* v. *Edenton-Chowan Bd. of Ed.,* 530 F.2d 567, 574 (4th Cir. 1975) (citing cases); and inaction may waive a separation-of-functions disqualification claim, *International Paper Co.* v. *FPC,* 438 F.2d 1349, 1357 (2d Cir.), *cert. denied,* 404 U.S. 827 (1971); *Democrat Printing Co.* v. *FPC,* 202 F.2d 298 (D.C. Cir. 1952); see *Satterfield* v. *Edenton-Chowan Bd. of Ed., supra; Duffield* v. *Charleston Area Medical Center, supra.* Under Section 3.42(g)(2) of the Commission's Rules of Practice, a party "may" choose to present a disqualification challenge; it need not do so. However, if it chooses to do so, it must do so promptly after the facts supporting the charge are known to it. A disqualification challenge to an ALJ's participation subsequent to the Commission's final decision based on circumstances known to a party before the Commission's final decision is not timely. *Capitol Transp., Inc.* v. *United States, supra; International Paper Co.* v. *FPC, supra; Safeway Stores, Inc.* v. *FTC, supra.*

The reasons supporting such a rule are manifold. A contrary holding, *inter alia,* would allow a party the possibility of invalidating the proceedings retroactively, unilaterally, and at will, if it feared or received an unfavorable ruling, or merely wished to delay the proceedings; might cause substantial delays, and, if retrial were required, significant unnecessary duplication of effort and expenditure of resources; and might make determinations of disqualification more difficult and less certain because of the passage of time. See generally *Marcus* v. *Director, Office of Wkrs.' Comp. Prog., supra,* 548 F.2d at 1050–51; *Duffield* v. *Charleston Areas Medical Center, supra.*

Applying these principles to this case, it is clear that the facts are substantially different from those in *Grolier.* In *Grolier,* the respondents in the Commission's adjudicative proceedings raised the issue promptly after Judge von Brand's record announcement of his prior service as attorney-advisor to Commissioner MacIntyre; both the ALJ and the Commission considered the claims promptly, during trial and before the closing of the record. Despite the ALJ's and the Commission's interlocutory rulings, the Grolier respondents pressed their claim—as was their right—on appeal of the initial decision to the Commission and on appeal of the Commission's decision to the Ninth Circuit. Moreover, the Grolier respondents never agreed not to present their disqualification claims.

In this case, Judge von Brand formally notified the parties on February 23, 1977, of his prior service to Commissioner MacIntyre. It is thus clear that, in the event that respondents did not know of Judge von Brand's service to Commissioner MacIntyre as of the time of Judge von Brand's appointment as an ALJ or as of the time the Commission issued its interlocutory order in *Grolier* in 1976, they did know of it at least nine months before trial began. Respondents agreed to put forward no objection, and, indeed, honored that agreement throughout the administrative trial and appeal of this case. Consistent with the above-cited authorities, which require timeliness in a disqualification application, respondents may not now for the first time raise this issue.

Of course, respondents do not contend that their failure to object—indeed, their agreement not to object—was predicated upon the Commission's 1976 *Grolier* ruling. Rather, they only suggest, in an indirect manner, that their failure to raise the issue at oral argument in July, 1979 was based on their reliance on *Grolier.* Yet, after the Ninth Circuit's decision in *Grolier,* they waited months before presenting any objection. During this time, the Commission issued its final order and opinion. Accordingly, even assuming that

an objection might have been timely after the Ninth Circuit's decision in *Grolier,* it is untimely now.

Finally, we note that respondents have not demonstrated or even asserted that they were prejudiced by any bias or reliance on extra-record materials by Judge von Brand; our review of the record convinces us that Judge von Brand was impartial in every respect, that his decision was thoroughly researched, and that his meticulous findings and conclusions were firmly and exclusively based on the record evidence. Of course, to the extent respondents challenged Judge von Brand's findings, conclusions, and proposed order, we undertook an exhaustive, independent review. In that review, we did not find that issues of demeanor or discretion were especially important in the determination of the case; thus, even if it were to be determined that Judge von Brand was disqualified, our decision of April 30, 1980, would not be void, as respondents have neither demonstrated nor suggested actual prejudice from his presiding, and we perceive none.[5] See Attorney General's Manual on the Administrative Procedure Act at 73–74 (1974).

For the foregoing reasons, respondents' motion for reconsideration based upon Judge von Brand's participation is denied.

C.

Finally, respondents assert that the Commission took various actions in this adjudication and in the investigation preceding it at times when the Commission was without authority and without appropriated funds, and, consequently, that the Commission violated the Antideficiency Act. Respondents assert that the Commission should either declare the entire adjudicatory proceeding void or remand the proceeding to the Administrative Law Judge to allow discovery by respondents as to the Commission acts performed during periods of lapsed appropriations.

The Antideficiency Act, 31 U.S.C. 655(a) (1976), prohibits any government officer or employee, unless expressly authorized by statute, from incurring any obligation on the part of the United States to pay money in advance of appropriations for that purpose.

[5] Ironically enough, at another point in this proceeding, Judge von Brand suggested to the parties that it might be necessary or advisable to have another ALJ assigned to this case because of his heavy case load. When asked for his reaction to this possibility, counsel for Herbert R. Gibson, Sr., and Herbert R. Gibson, Jr., told Judge von Brand "We'd like to keep you." Tr. at 276.

Although the Commission's funding did lapse during several of the periods listed by respondents in their petitions for reconsideration,[6] the legal validity of the Commission's actions is unaffected by the temporary lapse of appropriations for the following reasons.

First, actions by Commission employees completed prior to the expiration of appropriations do not create an unfunded obligation and, therefore, do not result in a violation of the Antideficiency Act.

Second, even if a Commission action on the *Gibson* matter was not completed prior to the expiration of appropriations and, therefore, were to be interpreted as incurring a Commission obligation, such action was ratified by Congress when the Commission's funding was made retroactive either explicitly or implicitly to the start of the period of lapsed appropriations.[7] As noted in the recent opinion letter of the Attorney General, on which respondents rely, such a ratification has the effect of providing legal authority for agency actions, even where there was none before. Letter from Attorney General Benjamin Civiletti to President Jimmy Carter (April 25, 1980). Thus, even assuming that respondents have standing to challenge the Commission actions,[8] none of the Commission's activities has been invalidated by the Antideficiency Act.

In this respect, too, therefore, the petitions for reconsideration are denied.

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[6] Contrary to respondents' assertion, the Commission's funding did not lapse during the periods July 1–September 30, 1976, and March 12–March 15, 1980. See Public Laws 94–121 and 96–123, respectively. The former period, in particular, related not to a lapse in funding, but to a change in the United States Government's fiscal year.

[7] See Public Laws 93–118, 93–124, 93–448, 93–563, 95–431, 96–86, and 96–219.

[8] Neither the Antideficiency Act itself nor its legislative history or scheme suggests that private persons are to be afforded a remedy under the Act. The language of the statute specifies that a government officer or employee who violates Sections 665(a) or (b) of the Act will be subjected to administrative and/or criminal penalties. 31 U.S.C. 665(i)(1). Moreover, the legislative history clearly indicates that the intended beneficiary of the regulatory scheme was Congress; the statutory scheme was designed to require the careful apportionment by Federal agencies of the funds distributed by Congress and thereby ensure the efficient administration of the government's business.

IN THE MATTER OF

CHRYSLER CORPORATION

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-3033. Complaint, Aug. 12, 1980—Decision, Aug. 12, 1980

This consent order requires, among other things, a Highland Park, Mich. manufacturer of motor vehicles to cease failing to notify owners of 1976/1977 Aspens and Volares, purchased or driven in specified states and locales, of the availability of replacement and reimbursement programs for premature rusting; remove and replace, without charge, the front fender(s) of vehicles that began to experience premature rusting within 36 months-in-service; and reimburse owners of affected vehicles for costs incurred in attempting to correct the premature rusting problem. The manufacturer is further required to notify dealers, in writing, of the existence of premature rusting; supply them with an adequate supply of replacement parts; and inform them of the firm's obligations under the terms of the order.

Appearances

For the Commission: *Aaron H. Bulloff, Richard H. Gateley, David Montgomery, Noble F. Jones* and *David V. Plottner.*

For the respondent: *Robert T. Talbot-Stern,* Detroit, Mich.

COMPLAINT

Having reason to believe that Chrysler Corporation, a corporation, has violated Section 5 of the Federal Trade Commission Act, and that a proceeding against it would be in the public interest, the Federal Trade Commission issues this complaint stating its charges. This complaint is issued pursuant to the provisions of and by virtue of the authority granted by the Federal Trade Commission Act.

PARAGRAPH 1. Respondent Chrysler Corporation is a Delaware corporation. Respondent's address is 12000 Lynn Townsend Drive, Highland Park, Michigan.

PAR. 2. Respondent is now, and has been, engaged in the manufacture, advertising, sale, and distribution of motor vehicles.

PAR. 3. Respondent causes motor vehicles to be shipped to purchasers in various states, and therefore maintains, and at all times mentioned in this complaint has maintained, a substantial course of trade in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act.

PAR. 4. For the purpose of this complaint, "premature rusting"

shall mean rusting which may perforate the top rear portion of the front fenders of 1976 and 1977 model year Aspens and Volares. Rusting attributable to normal deterioration as a result of age is excluded.

PAR. 5. Aspen and Volare vehicles produced from 1975 through 1977 are subject to premature rusting.

PAR. 6. Notwithstanding its knowledge since 1977 of premature rusting, respondent has failed, and is failing, to disclose to owners of Aspen and Volare vehicles the possibility of premature rusting, and the nature and extent of repairs necessary to correct such rusting. Respondent's failure to disclose this information to owners of vehicles subject to such rusting may cause owners substantial economic harm due to their inability to avoid or prevent premature rust. Such failure to disclose is an unfair or deceptive act or practice.

PAR. 7. In some cases, when owners have complained of premature rusting, respondent has provided replacement fenders free of charge. In other cases, respondent has provided replacement fenders free of charge and has paid labor costs for installing replacement fenders. In most instances, however, owners are not compensated because they are unaware of respondent's actions with respect to providing replacement fenders free of charge or paying labor costs.

PAR. 8. Respondent has failed, and is failing, to disclose to owners of Aspen and Volare vehicles its actions with respect to providing replacement fenders free of charge or paying labor costs. Respondent's failure to disclose such actions to owners of affected vehicles may cause them substantial economic harm by denying them an opportunity to request compensation from respondent. Such failure to disclose is an unfair or deceptive act or practice.

PAR. 9. Respondent's acts and practices, as alleged in this complaint, were and are all to the prejudice and injury of the public and constitute unfair or deceptive acts or practices in or affecting commerce, in violation of Section 5 of the Federal Trade Commission Act.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the Cleveland Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act; and

The respondent, its counsel, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter, and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, and having duly considered the comments filed thereafter by interested persons pursuant to Section 2.34 of its Rules, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following Order:

1. Respondent Chrysler Corporation is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its office and principal place of business located at 12000 Lynn Townsend Drive, in the City of Highland Park, State of Michigan.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

Order

For the purposes of this Order, the following definitions shall apply:

1. "Motor vehicle(s)" shall mean all 1976 and 1977 model year Aspens and Volares.

2. "Premature rusting" shall mean the presence of holes, blisters or bubbles in exterior paint caused by rust in the top rear portion of the front fender(s) of motor vehicles within two feet of the rear edge of such fender(s).

3. "Dealer(s)" shall mean any person(s), partnership(s), firm(s), or corporation(s) which, pursuant to a sales and service agreement with respondent receives on consignment or purchases motor vehicles from respondent for resale or lease to the public, including

any person(s), partnership(s), firm(s), or corporation(s) owned or operated by respondent.

4. "Owner" shall mean any person, partnership, firm, or corporation having custody and/or possession of a motor vehicle, including those vehicles held for resale.

5. "Remove and replace" shall mean removing any front fender affected by premature rusting and replacing it with a new, one-side galvanized front fender; *provided that* if such replacement fender is not available due to circumstances beyond respondent's control, respondent may substitute a zincrometal front fender. Also included in this term is the labor necessary to hang and paint the replacement front fender and to affix trim and accessory items, including splash shields.

6. "Months-in-service" shall be calculated as beginning on the date on which Chrysler began warranty coverage on the motor vehicle. If the date on which warranty coverage began ("in-service" date) cannot be established by Chrysler, then such date shall be calculated as beginning on:

October 1, 1976, for any 1976 model year motor vehicle;

October 1, 1977, for any 1977 model year motor vehicle.

I

It is ordered, That respondent Chrysler Corporation, a corporation, its successors and assigns, and its officers, agents, representatives, and employees, directly or indirectly or through any corporation, subsidiary, division, or other device, in connection with the manufacture, advertising, offering for sale, sale or distribution of vehicles in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended, do forthwith cease and desist from:

A. Failing to send by first-class mail, within sixty (60) days after the date of service of this Order, a copy of the letter attached to this Order as Attachment A, incorporated herein by reference, a form approved by the Federal Trade Commission, and a self-addressed, postage-paid envelope. This material shall be sent in one envelope similar in all material respects to Attachment B of this Order, incorporated herein by reference. The letter, form, and self-addressed, postage-paid envelope shall be mailed to each owner of a motor vehicle registered in any of the following states or localities, and to each owner of a motor vehicle purchased in any of the said

336-345 O - 81 - 10

states or localities, even though the vehicle is no longer registered in that state or locality.

All counties within the states of:

Connecticut	New Hampshire
Delaware	New Jersey
Illinois	New York
Indiana	Ohio
Iowa	Pennsylvania
Maine	Rhode Island
Massachusetts	Vermont
Michigan	Wisconsin

The following counties in Maryland, Minnesota and West Virginia:

Maryland

Allegheny	Garrett

Minnesota

Anoka	Mower
Blue Earth	Nicollet
Carlton	Olmsted
Carver	Pine
Chisago	Ramsey
Dakota	Rice
Dodge	Scott
Faribault	Sherburne
Fillmore	Sibley
Freeborn	Steele
Goodhue	Wabasha
Hennepin	Waseca
Houston	Washington
Isanti	Winona
LeSueur	Wright
McLeod	

West Virginia

Brooke	Monongalia
Hancock	Ohio
Marion	Preston
Marshall	Wetzel

B. Failing to remove and replace the front fender(s) of any motor vehicle at no cost to the owner within one hundred twenty (120) days after the owner initially contacts respondent or a dealer, *provided that* respondent may require any owner to sign a statement, approved by the Federal Trade Commission, that the vehicle began to experience premature rusting within thirty-six (36) months-in-service.

C. Failing to reimburse any owner of a motor vehicle for the actual or the usual and customary charges in the owner's trade area, whichever is lower, for parts and labor for front fender repairs or replacements made at the owner's expense which eliminated, or were made in an attempt to eliminate, premature rusting, *provided that* respondent may require any owner to sign a statement, approved by the Federal Trade Commission, that the vehicle experienced premature rusting within thirty-six (36) months-in-service and to furnish reasonable evidence of repair or replacement. Such reimbursement shall be made within sixty (60) days after the owner initially contacts respondent or a dealer. For owners who were sent the letter and form pursuant to paragraph A of part I of this Order, such repairs or replacements must have been made prior to an owner's receipt of the letter and form.

D. Failing to provide all dealers with adequate supplies of front fenders and any other items necessary to effectuate removal and replacement.

E. Failing to provide all dealers with adequate supplies of unsigned statements referenced in paragraphs B and C of part I of this Order.

F. Failing to notify all dealers in writing within ten (10) days after the date of service of this Order of the existence of premature rusting, of the necessity for using galvanized front fenders or zincrometal front fenders and of the terms and conditions of respondent's obligations under this Order.

II

It is further ordered, That respondent's obligations under paragraphs B and C of part I of this Order shall not extend to those owners who initially contact respondent or a dealer after November 1, 1980, or after 42 months-in-service, whichever date is later.

III

It is further ordered, That respondent maintain documents demonstrating compliance with this Order for a period not less than three

(3) years. Such documents shall be made available to the Commission or its staff for inspection and copying upon reasonable request, and shall include, but are not necessarily limited to, those revealing:

A. The name and last known address of each owner who was sent the disclosures required by paragraph A of part I of this Order.

B. The name and last known address of each owner who requested repairs or reimbursement for repairs for premature rusting.

C. The name and last known address of each owner whose motor vehicle was repaired or who was reimbursed for repairs as required by paragraphs B and C of part I of this Order.

D. Communications with respondent concerning repairs or reimbursements for repairs made to motor vehicles affected by premature rusting.

E. Each instance arising under paragraph C of part I of this Order where Chrysler reimbursed an owner of a motor vehicle for less than one hundred percent (100%) of the actual charges for parts and labor, and those documents revealing the underlying basis for determining the usual and customary charges in each such instance.

F. Each instance arising under paragraphs B or C of part I of this Order involving a dispute over months-in-service, unless Chrysler determined to remove or replace front fenders or reimburse an owner in accordance with said paragraphs, notwithstanding the fact that the vehicle allegedly exceeded thirty-six (36) months-in-service.

G. Each instance arising under paragraph B of part I of this Order when Chrysler failed to remove and replace the front fenders of any motor vehicle, and each instance arising under paragraph C of part I of this Order when Chrysler failed to reimburse any owner of a motor vehicle, and those documents revealing the underlying basis for such failures.

IV

It is further ordered, That respondent shall, within sixty (60) days after the date of service of this Order, and at one year intervals thereafter through 1982, file with the Commission a report, in writing, signed by respondent, setting forth in detail the manner and form in which it has complied with this Order.

V

It is further ordered, That respondent notify the Commission at least thirty (30) days prior to any proposed change in the corporate

respondent, such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries, or any other change in the corporation which may affect compliance obligations arising out of this Order.

ATTACHMENT A
SERVICE & PARTS DIVISION

CHRYSLER CORPORATION

Dear Aspen or Volare owner:

Chrysler Corporation has a continuing interest in the quality of its cars. We have become aware of a condition in some 1976 and 1977 Aspens and Volares which you should know about. This condition may cause the front fenders of your Aspen or Volare to rust prematurely. In areas where roads are heavily salted, the condition is aggravated. Replacing front fenders is costly. By agreement with the Federal Trade Commission, Chrysler will replace your front fender(s) free or repay you for past repairs if:

(a) your front fender(s) is rusted in the affected area, as described below; and

(b) this rust appears(ed) within the car's first 36 months-in-service; and

(c) you contact Chrysler or your dealer before November 1, 1980, or before 42 months-in-service, whichever is later.

CHRYSLER'S REPLACEMENT/REPAY PROGRAM

1. Description Of The Front Fender Rust Condition

The rust problem occurs on the top horizontal part of the fender, within approximately two feet of the windshield. The fender's design sometimes hindered proper priming in this area at the factory. The rust starts on the front fender's underside. It appears first as bubbles or blisters in the paint. Soon, holes appear. The drawing at the end of this letter shows the problem area.

2. What Is "Months-in-Service"?

The "36 months-in-service" limitation and the "42 months-in-service" claim limitation start the day Chrysler began warranty coverage on your car. This "in-service" date appears on the attached form.

3. What You Do If The Rust Appears On A Fender Now

(a) Determine if the rust is in the front fender area described in paragraph 1. Also determine if the rust appeared during your car's first 36 months-in-service.

(b) If so, call any Dodge, Plymouth or Chrysler new car dealer to request free fender replacement.

(c) When an appointment has been arranged, bring the enclosed form to the dealer. Your car's fenders will be inspected. You will be asked to sign the statement on the repair part of the form certifying that the premature rust appeared within your car's first 36 months-in-service. If you qualify, the dealer will then arrange to have a new fender installed within 120 days of your request.

4. What You Do If The Rust Does Not Appear On A Front Fender Now, But Appears In The Future

Not all 1976 or 1977 Aspen or Volare front fenders will rust prematurely. But, just in case your car's front fenders rust in the future (but within 36 months-in-service), keep this letter and the form with the car. Then, you do (a), (b) and (c) in paragraph 3.

(If you sell your car, please give this letter and the form to the next owner.)

5. What You Do If You Paid For Front Fender Rust Repairs Yourself Before You Got This Letter

(a) Determine if the rust is in the front fender area described in paragraph 1. Also determine if the rust appeared during your car's first 36 months-in-service.

(b) Carefully read the statement (in the repayment part of the form) about when the rust first appeared on your car's front fender. If the rust occurred during the car's first 36 months-in-service, sign the statement and mail it with your original repair bills (keep a copy for yourself), copies of cancelled checks, or other proof that repairs were done, to the address shown. If you do not have your original bill, try to get one from the repair shop. If you cannot get an original, send a copy.

(c) Chrysler will repay you for reasonable repair bills. (Chrysler may wish to see your car and proof of payment before repaying you.)

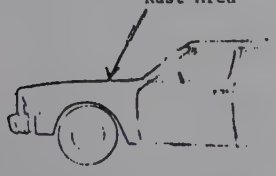
6. What You Should Remember

Chrysler's replacement program covers you only if you call or go to a Dodge, Plymouth or Chrysler dealer. Chrysler's repay program covers you only if you had repairs before you got this letter. In either case, you should act promptly after the rust appears.

Keep in mind that where road salt is used heavily our dealers' shops may be overcrowded. Also, matching paints exactly is not always possible. We deeply regret any inconvenience to you. We will handle each situation as quickly and fairly as possible. If you lose your form or if you have any problems with our program, call your local Chrysler Corporation Zone Office (listed in your Yellow Pages or Owner's Manual), or write to:

Chrysler Corporation
Service and Parts Division
Post Office Box 1718
Detroit, Michigan 48288

If you have difficulty finding your local Chrysler Corporation Zone Office phone number, you may call (313) 956-5970.



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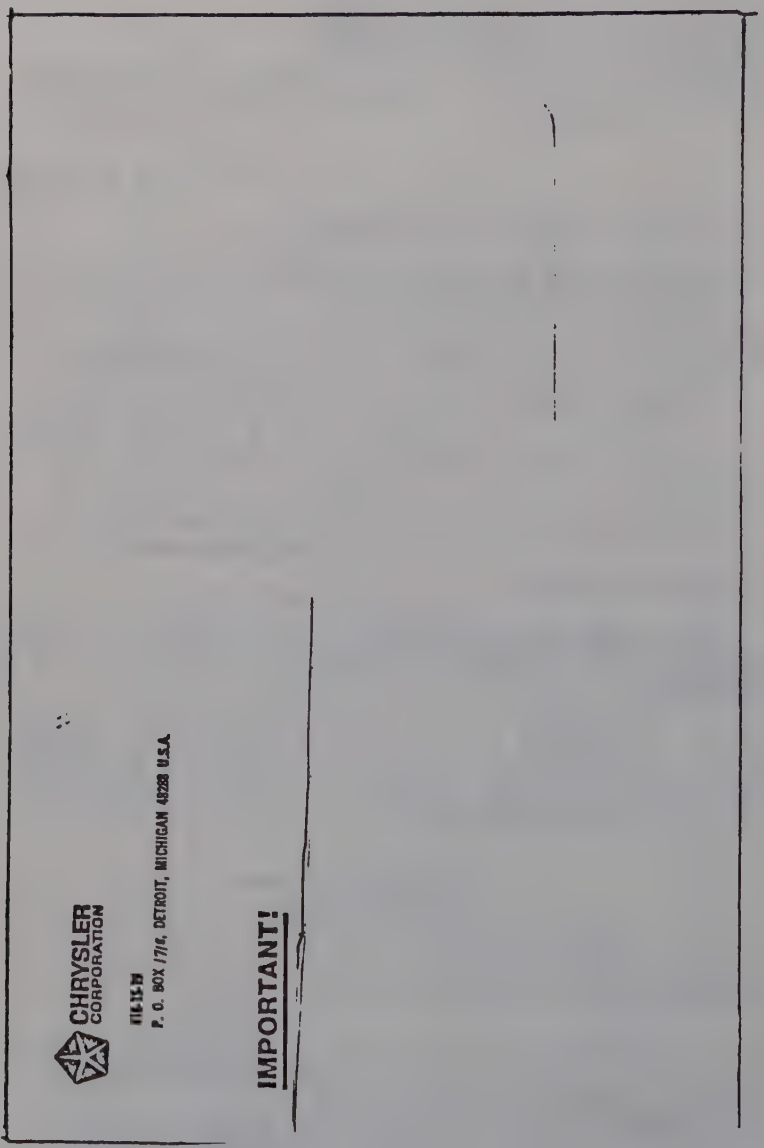
C. W. JOINER
General Manager -
Service and Parts Division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IMPORTANT!

In the Matter of

DARVEL, INC.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-3034. Complaint, Aug. 12, 1980—Decision, Aug. 12, 1980

This consent order requires, among other things, a Bellgarden, Calif. manufacturer and distributor of wearing apparel and related accessories to cease fixing or otherwise controlling the resale prices at which its products are sold or advertised; seeking the identity of dealers who fail to adhere to suggested resale prices and sales periods; and taking any adverse action against them. Respondent is barred from restricting the lawful use of brand names and trademarks in the advertising and sale of its products, and from granting any consideration, service or benefit to any dealer because of the resale price that another dealer has advertised or sold a product. Additionally, the order prohibits the firm from suggesting retail prices for its products for a period of one year.

Appearances

For the Commission: *Jeffrey A. Klurfeld.*

For the respondent: *J. Eddstepp Jr., Gibson, Dunn & Crutcher,* Los Angeles, Calif. and *Hal L. Cofkey, Cofkey, Cofkey & Boxer,* Los Angeles, Calif.

Complaint

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that Darvel, Inc., a corporation, hereinafter sometimes referred to as respondent, has violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges as follows:

For purposes of this complaint, the following definitions shall apply:

"Product" is defined as any item of wearing apparel or related accessory which is manufactured, offered for sale or sold by respondent.

"Dealer" is defined as any person, partnership, corporation or firm which sells any product in the course of its business.

"Resale Price" is defined as any price, price floor, price ceiling, price range, or any mark-up, formula or margin of profit used by any

dealer for pricing any product. Such term includes, but is not limited to, any suggested, established or customary resale price as well as the retail price in effect at any dealer.

"Sale Period" is defined as any time during which any dealer offers to sell any product at resale prices lower than those in effect during the usual and ordinary course of said dealer's business; or any suggested, authorized or customary time for selling or advertising any product at prices lower than the suggested, established or customary resale prices.

PARAGRAPH 1. Respondent Darvel, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of California, with its office and principal place of business located at 6891 Florence Place, Bellgarden, California.

PAR. 2. Respondent is now, and for some time last past, has been engaged in the manufacture, advertising, offering for sale, sale and distribution of wearing apparel and related accessories. Sales by respondent for fiscal year 1978 exceeded $6 million.

PAR. 3. Respondent maintains, and has maintained, a substantial course of business, including the acts and practices as hereinafter set forth, which are in or affect commerce, as "commerce" is defined in the Federal Trade Commission Act.

PAR. 4. Respondent sells and distributes its products directly to more than 2,000 retail dealers located throughout the United States who in turn resell respondent's products to the general public.

PAR. 5. In the course and conduct of its business, and at all times mentioned herein, respondent has been, and now is, in substantial competition in or affecting commerce with corporations, firms and individuals engaged in the manufacture, advertising, offering for sale, sale and distribution of merchandise of the same general kind and nature as merchandise manufactured, advertised, offered for sale, sold and distributed by respondent.

PAR. 6. In the course and conduct of its business as above described, respondent has for some time last past effectuated and pursued a policy throughout the United States, and has employed various means and methods in furtherance thereof, the purpose or effect of which is and has been to fix, control, establish, manipulate and maintain the resale prices at which its dealers advertise, offer for sale and sell its products.

PAR. 7. The aforesaid acts and practices of respondent have been and are now having the effect of hampering and restraining competition in the resale and distribution of respondent's products, and, thus, are to the prejudice and injury of the public, and constitute unfair methods of competition in or affecting commerce or

unfair acts and practices in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act. The acts and practices of respondent as herein alleged, are continuing and will continue in the absence of the relief herein requested.

Decision and Order

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the San Francisco Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act; and

The respondent, its attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent Darvel, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of California, with its office and principal place of business located at 6891 Florence Place, in the City of Bellgarden, State of California.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

Order

For the purposes of this Order, the following definitions shall apply: .

"Product" is defined as any item of wearing apparel or related

accessory which is manufactured, offered for sale or sold by respondent.

"Dealer" is defined as any person, partnership, corporation or firm which sells any product in the course of its business.

"Resale Price" is defined as any price, price floor, price ceiling, price range, or any mark-up, formula or margin of profit used by any dealer for pricing any product. Such term includes, but is not limited to, any suggested, established or customary resale price as well as the retail price in effect at any dealer.

"Sale Period" is defined as any time during which any dealer offers to sell any product at resale prices lower than those in effect during the usual and ordinary course of said dealer's business; or any suggested, authorized or customary time for selling or advertising any product at prices lower than the suggested, established or customary resale prices.

It is ordered, That respondent Darvel, Inc., a corporation, its successors and assigns, and respondent's officers, agents, representatives and employees, directly or indirectly, or through any corporation, subsidiary, division or other device, in connection with the manufacture, advertising, offering for sale, sale or distribution of any product in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from:

I

1. Fixing, establishing, controlling or maintaining, directly or indirectly, the resale price at which any dealer may advertise, promote, offer for sale or sell any product, or the sale period of any dealer.

2. Requesting, requiring or coercing, directly or indirectly, any dealer to maintain, adopt or adhere to any resale price or sale period.

3. Requesting or requiring, directly or indirectly, any dealer to report the identity of any other dealer who deviates from any resale price or sale period; or acting on any reports or information so obtained by threatening, intimidating, coercing or terminating said dealer.

4. Requesting or requiring that any dealer refrain from or discontinue selling or advertising any product at any resale price.

5. Hindering or precluding the lawful use by any dealer of any brand name, trade name or trademark of respondent in connection with the sale or advertising of any product at any resale price.

6. Making any payment or granting any consideration, service or

benefit to any dealer because of the resale price at which any other dealer has advertised or sold any product.

7. Conducting any surveillance program to determine whether any dealer is advertising, offering for sale or selling any product at any resale price, where such surveillance program is conducted to fix, maintain, control or enforce the resale price at which any product is sold or advertised.

8. Terminating or taking any other action to restrict, prevent or limit the sale of any product by any dealer because of the resale price at which said dealer has sold or advertised, is selling or advertising, or is suspected of selling or advertising any product.

II

1. For a period of one (1) year from the date of service of this Order, orally suggesting or recommending any resale price or sale period to any dealer.

2. For a period of one (1) year from the date of service of this Order, communicating in writing any resale price or sale period to any dealer; *provided, however,* that after said one (1) year period, respondent shall not suggest any resale price or sale period on any list, or in any advertising, book, catalogue or promotional material, unless it is clearly and conspicuously stated on each page where any suggested resale price or sale period appears, the following:

THE [RESALE PRICES OR SALE PERIODS] QUOTED HEREIN ARE SUGGESTED ONLY. YOU ARE FREE TO DETERMINE YOUR OWN [RESALE PRICES OR SALE PERIODS].

III

It is further ordered, That respondent shall within ninety (90) days after service of this Order, mail a copy of the enclosure set forth in the attached Exhibit A to each of its present accounts. An affidavit shall be sworn to by an official of the respondent verifying that the attached Exhibit A was so mailed.

IV

It is further ordered, That respondent shall forthwith distribute a copy of this Order to all operating divisions of said corporation, and to present or future personnel, agents or representatives having sales, advertising or policy responsibilities with respect to the subject matter of this order, and that respondent secure from each such person a signed statement acknowledging receipt of said Order.

V

It is further ordered, That respondent notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondent, such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporation which may affect compliance obligations arising out of the Order.

VI

It is further ordered, That respondent shall within sixty (60) days after service upon it of this Order, file with the Commission a report, in writing, setting forth in detail the manner and form in which it has complied with this Order.

EXHIBIT A

Dear Retailer:

Without admitting any violation of the law, Darvel, Inc. has agreed to the entry of an Order by the Federal Trade Commission regulating certain distribution practices. In connection therewith, the Company is required to send you this letter describing the Order.

The Order provides, among other things, as follows:

1. You can advertise and sell Darvel and Zepplin products at any price you choose.
2. Darvel will not take any action against you, including termination, because of the price at which you advertise or sell Darvel and Zepplin products.
3. Darvel will not suggest retail prices for any product until [1 year from the date of service of the Order].
4. The price at which you sell or advertise Darvel or Zepplin products will not affect your right to use Darvel or Zepplin trademarks or other identification in your sale or advertising of products bearing Darvel or Zepplin trademarks or identification.

If you have any questions regarding the Order or this letter, please call _____

_____

for Darvel, Inc.

IN THE MATTER OF

BRUNSWICK CORPORATION, ET AL.

FINAL ORDER, OPINION, ETC., IN REGARD TO ALLEGED VIOLATION OF SEC. 7 OF THE CLAYTON ACT AND SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT

Docket 9028. Complaint, April 15, 1975 —Final Order, August 14, 1980*

This order requires, among other things, a Skokie, Ill. manufacturer and marketer of outboard motors and other products and its subsidiary, Mariner Corp., to dissolve their joint venture agreement with Yamaha Motor Co., Ltd. ("Yamaha"); sell all their interests in Sanshin Kogyo Co., Ltd. to Yamaha, within 90 days; and remove their representatives on Sanshin's board of directors immediately. Further, the firms are prohibited for three years from acquiring, without prior Commission approval, any interest in a company manufacturing outboard motors for sale in the United States.

Appearances

For the Commission: *Steven R. Newborn.*

For the respondents: *Henry Y. Ota, Mori & Ota,* Los Angeles, Calif., *James H. Wehrenberg,* Skokie, Ill., *Mindy Liss, Mayer, Brown & Platt,* Wash., D.C., and *John R. Ferguson, Pettit & Martin,* Wash., D.C.

FINAL ORDER

For the purposes of this Order:

a) "Brunswick" shall mean the Brunswick Corporation, together with its present and future domestic and foreign subsidiaries, affiliates, joint ventures, related corporations (including Mariner Corp.), and corporations controlled by Brunswick Corporation; and all successors to Brunswick Corporation and their domestic and foreign subsidiaries, affiliates, joint ventures and related corporations; and all corporations controlled by the successors of Brunswick Corporation.

b) "Yamaha" shall mean Yamaha Motor Co., Ltd., together with its present and future domestic and foreign subsidiaries, affiliates, joint ventures, related corporation, and corporations controlled by Yamaha Motor Co., Ltd.; and all successors to Yamaha Motor Co., Ltd. and their domestic and foreign subsidiaries, affiliates, joint

* Complaint, Initial Decision, Opinion of the Commission, and Order Remanding for Additional Evidence previously published in 94 F.T.C. 1174.

ventures and related corporations; and all corporations controlled by the successors of Yamaha Motor Co., Ltd.

c) "Mariner" shall mean Mariner Corp., together with its present and future domestic and foreign subsidiaries, affiliates, joint ventures, related corporations, and corporations controlled by Mariner Corp.; and all successors to Mariner Corp. and their domestic and foreign subsidiaries, affiliates, joint ventures and related corporations; and all corporations controlled by the successors of Mariner Corp.

I.

It is ordered, That within 90 days of the date this Order becomes final, Brunswick and Mariner shall sell to Yamaha, and Yamaha shall buy from Brunswick and Mariner, all capital stock, bonds, debentures, and other securities and other interests held by Brunswick and Mariner in Sanshin Kogyo Co., Ltd. ("Sanshin"). The purchase price shall be equal in dollars to the value of the net tangible assets per share, computed and adjusted to the last day of the six month term immediately preceding the date of the sale.

II.

It is further ordered, That, on or before 90 days from the date this Order becomes final, Brunswick, Yamaha, and Mariner shall rescind in all respects the Joint Venture Agreement, and the agreements attached thereto, entered into on November 21, 1972, and all agreements modifying the Joint Venture Agreement and the agreements attached thereto, shall consider them null and void, and shall cease and desist from observing or enforcing the terms of said agreements.

III.

It is further ordered, That from the date this Order becomes final, Brunswick and Mariner shall cease any and all representation on the board of directors of Sanshin, cease and desist from taking any steps to nominate, seat, or admit any representatives of Brunswick and Mariner to the board of directors of Sanshin, and cease and desist from exercising any of the rights of a shareholder of Sanshin except the right to receive dividends.

IV.

It is further ordered, That from the date this Order becomes final, neither Brunswick nor Mariner shall enter into, continue to be a party to, or enforce any agreement which in whole or in part prevents a manufacturer, seller, or distributor of outboard motors from manufacturing, selling, or distributing such motors in the United States, its territories or possessions.

V.

It is further ordered, That from the date this Order becomes final, Yamaha shall not enter into, continue to be a party to, or observe any agreement which in whole or in part prevents Yamaha from manufacturing, selling, or distributing outboard motors in the United States, its territories or possessions.

VI.

It is further ordered, That Brunswick, Yamaha, and Mariner shall, for a period of three years from the date this Order becomes final, cease and desist from acquiring, directly or indirectly, through subsidiaries or otherwise, without the prior approval of the Federal Trade Commission, all or any part of the stock or share capital of any concern, corporate or noncorporate, engaged in the production, distribution or sale of outboard motors in or for the United States, or capital assets pertaining to such production distribution or sale of such motors in or for the United States.

VII.

It is further ordered, That Brunswick, Yamaha, and Mariner notify the Federal Trade Commission at least 30 days prior to any proposed change in its corporate structure such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries, or any change in the corporation which may affect compliance obligations arising out of this Order.

VIII.

It is further ordered, That Brunswick, Yamaha, and Mariner shall within 120 days of the date this Order becomes final, submit in writing to the Federal Trade Commission a verified report setting forth in detail the manner and form in which Brunswick, Yamaha,

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and Mariner each intends to comply or has complied with this Order. Brunswick, Yamaha, and Mariner shall submit such other information as may from time to time be requested by the Commission.

Commissioner Bailey did not participate.

Opinion of the Commission

By Pitofsky, *Commissioner:*

The sole question here is the formulation of an appropriate order of relief. On November 9, 1979, we determined that a joint venture between Brunswick Corporation ("Brunswick") and Yamaha Motor Company, Limited ("Yamaha") violated Section 7 of the Clayton Act[1] and Section 5 of the Federal Trade Commission Act.[2] Since the Administrative Law Judge ("ALJ") had originally ordered the dismissal of the complaint, his initial decision lacked findings and recommendations on the issue of appropriate relief. We therefore remanded the proceeding to enable him to address those questions. Additional hearings were held on February 19 and 20, 1980, and on March 14, 1980, the ALJ issued his "Findings and Proposed Order." After considering briefs filed by Complaint Counsel, Brunswick and Yamaha we have determined to adopt the ALJ's findings and issue the proposed order, with the minor modification discussed below.[3]

I

We concluded, in our previous opinion, that the joint venture violated the antitrust laws on three theories: (1) it eliminated the potential competition likely to result from Yamaha's probable independent entry into the United States outboard motor market; (2) it eliminated the existing competition Yamaha provided in that market; and (3) it included collateral agreements unreasonably limiting competition between Yamaha and Brunswick. In remanding the proceeding, we instructed the ALJ to determine the most effective means of terminating the joint venture, nullifying the

[1] 15 U.S.C.18.

[2] 15 U.S.C.45.

[3] The following abbreviations are used herein:

IDF — Initial Decision Finding of Fact No.
RDF — Remand Decision Finding of Fact No.
CX — Complaint Counsel's Exhibit No.
CCRAB — Complaint Counsel's Remand Appeal Brief Page No.
BRRB — Brunswick's Remand Reply Brief Page No.

restrictive agreements, and restoring Yamaha as an actual and potential competitor in the U.S. outboard motor market.

In brief summary, the ALJ's proposed order recommended: (1) the rescission of the joint venture agreement and all collateral agreements;[4] (2) the sale to Yamaha of all Brunswick's stock in Sanshin, the jointly owned manufacturing facility of Yamaha and Brunswick;[5] and (3) a three year prohibition upon Brunswick's or Yamaha's acquisition of any competitor in the outboard motor market without the prior approval of the Commission.[6]

II

Our goal, in fashioning relief for a violation of Section 7, is "to restore, so far as practicable and equitable, the state of competition in the relevant market as it would have been but for the acquisition."[7] As we observed in remanding this question to the ALJ, "we cannot turn back the clock," but "we can seek to restore the market structure to that which existed at the time the venture was entered upon."[8] This joint venture violated the antitrust laws because it eliminated the actual and potential competition that Yamaha represented in the U.S. outboard motor market. A satisfactory remedy must restore Yamaha, to the extent possible, as an actual and potential competitor with approximately that competitive vigor, independence and strength that it possessed in 1972.

We agree with the ALJ's conclusion that this objective can be achieved only by a complete undoing of the joint venture. The joint venture agreement and all collateral agreements must be rescinded, and the Sanshin stock held by Brunswick must be resold to Yamaha.

Divestiture of the acquired firm is the familiar remedy for a merger found to lessen actual or potential competition in violation of Section 7.[9] As the Supreme Court observed in *United States* v. *du Pont & Co.*, 366 U.S. 316 (1961), "divestiture is peculiarly appropriate in cases of stock acquistions which violate Section 7 . . . The very words of Section 7 suggest that an undoing of the acquisition is a natural remedy."[10] By making the acquired firm an actual or potential competitor again, a divestiture order helps restore the market structure existing before the challenged acquisition. The

[4] Paragraph II

[5] Paragraph I

[6] Paragraph VI

[7] *Fruehauf Trailer Co.*, 68 F.T.C. 1167, 1168 (1965), *modified*, 69 F.T.C. 180 (1966).

[8] *Brunswick Corp.* [94 F.T.C. 1174 at 1278] [1979] Trade Reg. Rep. (CCH) (FTC Complaints and Orders) Para. 21,623 at 21,788.

[9] *See, e.g., United States* v. *El Paso Natural Gas Co.*, 376 U.S. 651 (1964); *United States* v. *du Pont & Co.*, 366 U.S. 316 (1961).

[10] *United States* v. *du Pont & Co.*, 366 U.S. 316, 328–29, (1961).

lessening of competition resulting from this joint venture, as we noted in our previous opinion, is "roughly equivalent" to that which would have resulted from Brunswick's acquisition of an actual or potential competitor.[11] Just as an order of divestiture would have been an appropriate remedy for such an acquisition, we conclude that an undoing of the transaction is appropriate here as well.

We cannot accept Brunswick's suggestion that the order of relief void the various joint venture agreements, but allow Brunswick to retain and vote its shares of Sanshin common stock. Although Brunswick would be guaranteed no representation on the board of directors under this proposed plan,[12] Yamaha's independence and vitality as a competitor might still be impaired. Brunswick's ownership of 38% of Sanshin's voting stock could enable Brunswick to hamper Sanshin's competitive efforts, making Sanshin a less effective competitor than it had been before the joint venture.

Yamaha owned a majority of Sanshin stock prior to the creation of the joint venture, enough to control most questions raised in votes at shareholder meetings.[13] Since Yamaha now owns only 38%, Brunswick could conceivably enlist sufficient support among the remaining 24% held by individual Japanese shareholders to create a majority on some issues or at least to extract significant compromise concessions from Yamaha. Moreover, under the Japanese Commercial Code and Sanshin's articles of incorporation, a two thirds vote is necessary to approve several significant types of corporate actions—a merger or acquisition, for example, a change in authorized capital, or the issuance of new shares of stock.[14] With respect to these questions, Brunswick's 38% of the outstanding stock would amount to an absolute veto.

Finally, aside from the possible influence or control resulting from Brunswick's ownership of Sanshin stock, that stock ownership would also provide Brunswick access to competitively sensitive information otherwise unavailable to competitors.[15] Brunswick's access to such information—profitability data, inventory schedules or new construction reports, for example—might significantly impair Sanshin's effectiveness as a competitor.

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[11] *Brunswick Corp.* [94 F.T.C. 1174 at 1268] [1979] Trade Reg. Rep. (CCH) (FTC Complaints and Orders) Para. 21,623 at 21,782.

[12] The present division of seats on the board of directors—five to Brunswick and six to Yamaha—is required by the joint venture agreement. *See* CX 1. If that agreement were voided, the directors would be elected by shareholders under Sanshin's articles of incorporation. *See* CX 1-Y. Since those articles do not provide for cumulative voting, Brunswick's 38% of the outstanding Sanshin stock is insufficient, alone, to elect any directors.

[13] Sanshin's articles of incorporation provide that: "Unless otherwise provided by law or by these Articles of Incorporation, all resolutions of meetings of shareholders shall be adopted by a majority of the voting rights present at the meeting." CX 1-X.

[14] *See* RDF 42-49.

[15] *See* RDF 53.

This possible lessening of competition resulting from Brunswick's ownership of 38% of Sanshin's common stock is, no doubt, more attenuated than that accompanying the original joint venture itself. Nonetheless, ample authority holds that Section 7 may be violated when an acquisition of less than a majority of a firm's stock creates the possibility that the acquiring firm either may gain access to confidential competitive information, or may be able to steer the acquired firm towards less competitive strategies.[16] Considering the record evidence that Brunswick has eagerly seized opportunities to minimize the competition provided by Sanshin—evidence that can be found in both the creation of this joint venture and in Brunswick's actions during its existence[17]—we conclude that the possible lessening of competition likely to result from allowing Brunswick to keep its Sanshin stock is far from insubstantial.

These same considerations dictate that an order requiring the divestiture of Brunswick's Sanshin stock to any buyer would also be an insufficient remedy; the stock must be sold to Yamaha. Divestiture of Brunswick's Sanshin stock to any other buyer would not restore Yamaha to its pre-joint venture competitive position. Yamaha would be left with only a minority holding of Sanshin stock, and not the controlling position it held prior to the joint venture. Without majority control, Yamaha might be unable to enter or compete effectively in the U.S. outboard motor market. Indeed, if Brunswick's Sanshin stock were divested to another competitor in that market, or ultimately come to rest in such a competitor's hands, competition might be lessened in much the same manner as if Brunswick retained the stock—that competitor might be able to influence Sanshin's decision-making, for example, or gain access to competitively sensitive information. We conclude, therefore, that fashioning a satisfactory remedy in this case—a remedy effectively restoring Yamaha as an actual and potential competitor—requires not only the voiding of the joint venture agreements, but the return of Brunswick's Sanshin stock to Yamaha as well.[18]

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[16] *See, e.g., United States* v. *du Pont & Co.*, 366 U.S. 316 (1961); *F&M Schaefer Corp.* v. *C. Schmidt & Sons, Inc.*, 597 F.2d 814 (2d Cir. 1979); *Gulf & Western Indus., Inc.* v. *Great Atlantic & Pacific Tea Co., Inc.*, 476 F.2d 687 (2d Cir. 1973); *American Crystal Sugar Co.* v. *Cuban-American Sugar Co.*, 259 F.2d 524 (2d Cir. 1958); *Hamilton Watch Co.* v. *Benrus Watch Co.*, 114 F.Supp. 307 (D. Conn.), *aff'd*, 206 F.2d 738 (2d Cir. 1953).

[17] The ALJ observed that Brunswick had effectively used its holdings of Sanshin stock and its position on Sanshin's board of directors to hinder any direct competition provided by Sanshin, and hence, Yamaha. *See, e.g.*, RDF 22, 23.

[18] No previous decision has ever addressed the problem of determining an appropriate remedy for a joint venture found to violate Section 7. Although consent decrees hold little precedential value, *see United States* v. *du Pont & Co.*, 366 U.S. 316, 330 n. 12 (1961), we note that consent decrees in such cases have ordered relief similar to that suggested here by the ALJ—the voiding of any joint venture agreement and the rescission of any stock acquisition. *See, e.g., Continental Oil Co.*, 72 F.T.C. 850 (1967) (consent order); *Phillips Petroleum Co.*, 70 F.T.C. 456 (1966) (consent order); *United States* v. *Monsanto Co.*, 1967 Trade Cas. Para. 72,001 (W.D. Pa. 1967) (consent decree). Courts have concluded that their equitable power encompasses an order directing the rescission of a stock

(Continued)

The provision governing the sale of Brunswick's stock in the ALJ's proposed order of relief differed from a simple order of rescission in one important respect. It ordered that Brunswick sell its Sanshin stock to Yamaha at a price different from that which Brunswick originally paid. Under the joint venture agreement executed in 1972, Brunswick purchased the newly issued Sanshin stock at a price equal to the "value of the net tangible assets per share" of Sanshin's then outstanding stock.[19] That value was calculated by a procedure outlined in the joint venture agreement.[20] Requiring Brunswick to receive the same dollar figure for its sale of the stock under this order might inflict substantial economic hardship; the value of the shares may have appreciated considerably during the intervening years.

The possibility of such hardship, of course, would not be sufficient reason to chose a less effective form of relief. As the Supreme Court noted in *United States* v. *du Pont & Co.*, 366 U.S. 316 (1961), once a conclusion has been reached "that other measures will not be effective to redress a violation, and that complete divestiture is a necessary element of effective relief, the Government cannot be denied the latter remedy because economic hardship, however severe, may result."[21] But the issue here is not a choice between an effective form of relief and a less effective one, but rather a question of how to implement the form of relief we have already determined to be most effective. We have decided that Brunswick's Sanshin stock must be sold to Yamaha; the question that remains is the appropriate price. In these circumstances, it is important to consider any hardship attendant upon our decree.[22]

No easy answer exists to this problem. The ALJ apparently concluded that any hardship could be minimized by defining the price as "the value of the net tangible assets per share, computed and adjusted to the last day of the six month term immediately preceding the date of the sale."[23] We affirm that conclusion. The

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acquisition violating Section 7. *See U.S.* v. *Coca-Cola Bottling Co. of L.A.*, 575 F.2d 222 (9th Cir.), *cert. denied*, 439 U.S. 959 (1978); *United States* v. *Reed Roller Bit Company*, 274 F.Supp. 573 (W.D. Okla. 1967). *See also U.S.* v. *Phillips Petroleum Co.*, 367 F.Supp. 1226 (C.D. Cal. 1973), *aff'd*, 418 U.S. 906 (1974). We believe that our remedial powers encompass no less. *See Ekco Products Co.* 65 F.T.C. 1163 (1964), *aff'd*, 347 F.2d 745 (7th Cir. 1965).

[19] CX 1-C.

[20] CX 1-C.

[21] *United States* v. *du Pont & Co.*, 336 U.S. 316, 327 (1961). One court of appeals, in affirming a district court's issuance of a preliminary injunction to preserve the ultimate availability of rescission as a remedy for an acquisition, observed that the possible unfairness to the acquiring company would not be reason to deny the remedy of rescission: "If nothing else, the buyers in this transaction . . . might be required to give back the illegally acquired assets . . . without accepting full repayment." *U.S.* v. *Coca-Cola Bottling Co. of L.A.*, 575 F.2d 222, 231 (9th Cir.), *cert. denied*, 439 U.S. 959 (1978).

[22] *See Ekco Products Co.*, 65 F.T.C. 1163, 1221 (1964), *aff'd*, 347 F.2d 745 (7th Cir. 1965) ("If the Commission enjoys, as we think it does, essentially equitable powers under Section 11 of the Clayton Act, it must, as a corollary, assume equitable responsibilities.")

[23] Paragraph I.

valuation formula chosen by the ALJ was the same one used by the parties to determine the price Brunswick initially paid for the Sanshin stock.[24] The arms length bargaining that occurred suggests some fairness in that formula.[25] Yet by requiring that the assets be valued near the time of the sale to Yamaha, rather than at the time of Brunswick's initial purchase, the order is likely to reduce any hardships resulting from changes in either Sanshin's assets or their value.[26]

III

In addition to the provisions voiding the joint venture agreements and ordering the divestiture of Brunswick's Sanshin shares, the ALJ's proposed order of relief contained a three year requirement that both Brunswick and Yamaha seek Commission approval before acquiring any firm engaged in the production, distribution or sale of outboard motors.[27] We consider that provision both an appropriate and necessary element of the relief in this case. The authority to include such a requirement in an order of relief cannot be questioned.[28] The sole issue—as it is with any element of a Commission remedial order—is whether this requirement of Commission approval of future acquisitions has some "reasonable relation" to the violations of Brunswick and Yamaha.[29] We conclude that it does.

Brunswick's acquisition of Sanshin stock presents the more typical instance of illegal conduct where this kind of relief is appropriate.[30] Commission review is necessary to insure that Brunswick does not again act to substantially lessen competition in the U.S. outboard motor market by acquiring an actual or potential competitor. Considering the thoroughness with which this joint venture was constructed to minimize the competition provided by Yamaha in the U.S. market, it is reasonable to predict that such a path could be followed again.

Although Yamaha's actions present a more unusual case—Yam-

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[24] CX 1–C.

[25] We cannot accept Brunswick's suggestion that the parties be allowed to negotiate a price for the sale. It is difficult to imagine fair bargaining once an order has required that the stock be sold.

[26] We reject Yamaha's suggestion that Sanshin's assets be valued as of October 31, 1979, the close of the accounting period immediately preceding the publication of our opinion finding that the joint venture violated Section 7. Since considerable time may pass before our order is effectuated, we believe that both parties should share in any appreciation in the value of Sanshin's assets.

[27] Paragraph VI.

[28] *See, e.g., Ekco Products Co.*, 65 F.T.C. 1163, 1215 (1964), *aff'd*, 347 F.2d 745 (7th Cir. 1965); *Abex Corp* v. *FTC*, 420 F.2d 928, 933 (6th Cir.), *cert. denied*, 400 U.S. 865 (1970).

[29] *See FTC* v. *Colgate-Palmolive Co.*, 380 U.S. 374, 394–5 (1965); *FTC* v. *National Lead Co.*, 352 U.S. 419, 429 (1957); *Jacob Siegal Co.* v. *FTC*, 327 U.S. 608, 612–13 (1946).

[30] *See, e.g., RSR Corp.*, 88 F.T.C.. 800 (1976), *aff'd*, 602 F.2d 1317 (9th Cir. 1979), *cert. denied*, 100 S. Ct. 1313 (1980); *Avnet, Inc.*, 82 F.T.C. 391 (1973), *aff'd*, 511 F.2d 70 (7th Cir.), *cert. denied*, 423 U.S. 833 (1975).

aha's violations consisted of participation in this joint venture through sale of stock and of agreement to various covenants not to compete—they nonetheless justify similar relief. A requirement of Commission approval of future acquisitions is especially valuable in the drafting of remedial orders seeking to insure that the possible procompetitive benefits of entry by a potential competitor are not lost.[31] In this case, a primary goal of the order of relief is to preserve the possible procompetitive benefits of Yamaha's potential entry into the U.S. outboard motor market. By participating in the joint venture with Brunswick, Yamaha chose to enter that market in a manner that substantially lessened competition. Requiring Yamaha to come before the Commission before entering the market by acquisition or joint venture is necessary to insure that future entry is not also anticompetitive.[32]

Though a requirement of Commission approval is appropriate here, we consider too broad the provision drafted by the ALJ. Yamaha, for example, has objected that the ALJ's order might hamper possible future acquisitions or joint ventures in Japan, or other foreign markets—legitimate competitive acts having no impact upon the U.S. outboard motor market. To allay such concern, we have narrowed the scope of the provision so that it applies only to acquisitions of the stock or assets of firms engaged in the production, distribution or sale of outboard motors "in or for the United States."

The ALJ's proposed order also contained provisions prohibiting both Brunswick and Yamaha from again entering mutual covenants not to compete—either with one another or with any other competitor in the U.S. outboard motor market.[33] We conclude that these provisions are also appropriate and necessary components of the order of relief. They prohibit the repetition of conduct we have found illegal—an example of the clearest reasonable relation of remedy to violation.[34] And, as we have already observed, in light of the record evidence it is not unreasonable to conclude that a danger of future anticompetitive conduct exists.[35]

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[31] *See, e.g., Ekco Products Co.*, 65 F.T.C. 1163, 1228 (1964), *aff'd*, 347 F.2d 745 (7th Cir. 1965).

[32] Drafting an effective order of relief often requires consideration of possible conduct not involved in the original violation: "When the purpose to restrain trade appears from a clear violation of the law, it is not necessary that all untravelled roads to that end be left open and that only the worn one be closed." *International Salt Co.* v. *U.S.*, 332 U.S. 392, 400 (1947). *See, e.g., FTC* v. *Colgate-Palmolive Co.*, 380 U.S. 374, 395 (1965) (discussing necessity of "fencing in" in advertising violations); *International Salt Co.* v. *U.S.*, 332 U.S. 392 (1947) (similar issues in tying violation).

[33] Paragraphs IV and V.

[34] *See, e.g., FTC* v. *Colgate-Palmolive Co.*, 380 U.S. 374 (1965).

[35] The ALJ's proposed order of relief also contained a provision requiring Brunswick and Yamaha to notify the Commission of significant changes in their corporate structure. Paragraph VII. This provision is necessary to ensure effective monitoring of Brunswick and Yamaha's compliance with the order.

IV

In our previous opinion remanding this proceeding, we instructed the ALJ to study the effect of a termination of this joint venture upon the ability of Mariner dealers to obtain satisfactory supplies of outboard motors. We cautioned that the achievement of an appropriate remedy in this case "should not be accomplished at the expense of the Mariner dealers if that is avoidable."[36]

On remand, Complaint Counsel argued that Mariner dealers would be satisfactorily protected only if the order of relief required Yamaha to continue to supply Mariner with "commercially reasonable quantities" of outboard motors until April 30, 1983, and of spare parts for those motors until April 30, 1990.[37] To insure that Yamaha would have the technology necessary to satisfy those supply obligations, Complaint Counsel also proposed provisions in the order of relief: (1) requiring royalty free grants between Brunswick and Yamaha of any patent rights or licenses utilized by the joint venture; and (2) establishing as joint property any other technical information exchanged during the joint venture.[38]

The ALJ concluded that neither the imposition of the supply requirements nor the grants of access to patented and nonpatented technology were necessary to protect Mariner dealers. We accept that conclusion. There is no convincing evidence in the record that Mariner dealers will be endangered by any sudden supply shortages. Sanshin presently sells 25% of its production to Mariner dealers.[39] It seems unlikely that Yamaha would readily relinquish so substantial a source of profit. And, even if Sanshin's sales to Mariner dealers did decrease somewhat, the record shows that Brunswick has long desired the capability of satisfying the needs of Mariner dealers from its own production, and has been preparing that capability throughout the life of the joint venture.[40] In light of this evidence we conclude that Mariner dealers face no significant danger from our termination of this joint venture.

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[36] *Brunswick Corp.*[94 F.T.C. 1174 at 1279] [1979] Trade Reg. Rep. (CCH) (FTC Complaints and Orders) ¶ 21,623 at 21,788.

[37] Paragraph VII of Complaint Counsel's Proposed Order. CCRAB, Attachment A, p. 3.

[38] Paragraph IV of Complaint Counsel's Proposed Order. CCRAB, Attachment A, p. 2.

[39] RDF 66.

[40] *See, e.g.*, IDF 199; RDF 74-77. Brunswick has taken the position on this appeal that it is "prepared to supply Mariner if necessary." BRRB p. 6.

IN THE MATTER OF

GENERAL FOODS CORPORATION

Docket 9085. Interlocutory Order, Aug. 18, 1980

ORDER DEFINING PERMISSIBLE SCOPE OF TESTIMONY OF WILLIAM H. SPRUNK UNDER QUARTERLY FINANCIAL REPORTS CONFIDENTIALITY RULES

By order of March 20, 1980, the Commission stayed, pending its review of the matter, the return on the subpoena issued to a Commission employee, William H. Sprunk, Assistant Director for Financial Statistics, Bureau of Economics. The purpose of the stay was for the Commission to review the interpretation and application of the confidentiality rules governing the Quarterly Financial Reports (QFR)[1] and Line of Business (LB)[2] programs to the subpoenaed testimony of an employee of the Commission's Division of Financial Statistics, Bureau of Economics, in a Commission adjudicative proceeding. The crux of the instant order is the resolution of the apparent conflict between Mr. Sprunk's permissible functions under the QFR and Line of Business confidentiality rules and his testimony in response to the adjudicative subpoena.

The complaint in this case alleges General Foods' use of pricing practices and other policies to the injury of competitors in eastern coffee markets. Complaint counsel's expert witness used data obtained from published aggregate data in the QFR survey to establish a benchmark as to the existence of monopoly power, one of the issues in the case. The subpoena *ad testificandum* for Mr. Sprunk, who heads the Division of Financial Statistics, in which the QFR report is prepared, was issued by the Administrative Law Judge in order to

> ha[ve] someone who knows what these figures are about testify as to the accuracy of the figures, how they are compiled, and why this contract was let to Standard and Poor's. [Tr. 5242][3]

The Commission's order staying the subpoena return invited

[1] 38 Fed. Reg. 18720, 26162 (1973).

[2] 41 Fed. Reg. 28041, 34703 (1976); 40 Fed. Reg. 21542, 22318 (1975); 39 Fed. Reg. 30970 (1974). The subpoena issued to Mr. Sprunk appears to concern only QFR data, and the Commission's LB confidentiality rules are relevant here only insofar as they might suggest that no employee of the Division of Financial Statistics may appear in an adjudicative proceeding for any purpose. The Commission's order does not reach issues concerning the admissibility of LB reports or the privileged status of individual company data obtained in the LB program. *See* note 8, *infra*.

[3] The transcript reflects discussion of a contract using a data tape prepared by Standard & Poor's leading to a "final report, including a statistical statement re QFR accuracy * * *." (Tr. 5237)

General Foods and complaint counsel to submit simultaneous memoranda on the following issues:

1. Whether response to a subpoena in a Commission adjudicative proceeding by an employee of the Division of Financial Statistics constitutes "engag[ing] in any activity of the Commission which involves regulation or investigation * * * "[4] or "participat[ion] in any Commission investigation or proceeding for carrying out specific law enforcement responsibilities of the Commission * * *,"[5] within the meaning of the prohibitions established by the QFR and LB confidentiality rules;

2. If such activity is appropriate, whether it nevertheless remains the case that an employee of the Division of Financial Statistics may not give an answer concerning the QFR program which would disclose "the names of companies, financial data, and all other information which are obtained from the respondent companies" (*i.e.,* individual company data) in connection with the QFR program; and

3. Whether substantial prejudice to any party will result if the confidentiality rules are interpreted as outlined in (1) and (2) above.

The first question posed in the Commission's order staying the subpoena return may be answered directly, and in the negative. The clear purpose of both the LB and QFR confidentiality rules is to ensure that the individual company data be kept confidential and used only for statistical purposes, and specifically, as stated in the Commission's QFR authorizing resolution, that the individual company data "not be available for use in any Commission adjudication or in connection with any investigation for the purpose of initiating adjudicative proceedings * * * ."[6] Both sets of rules prohibit employees of DFS, which in general has sole access to the data, from engaging in investigatory and law enforcement activities of the Commission. This division of internal agency functions is a preventative measure designed to avoid any appearance, or any remote possibility, that investigatory or enforcement decisions at the FTC would be made on the basis of individual company QFR or LB data. To the extent that Mr. Sprunk's testimony here would not be based on individual company QFR data, it would be consistent with the purpose of the confidentiality rules. Accordingly, insofar as the rules are concerned, Mr. Sprunk should be permitted to testify about matters such as the methods and procedures for compiling the QFR survey and its overall accuracy, but he should not be permitted to

[4] 38 Fed. Reg. at 26162 (1973).
[5] *E.g.,* 41 Fed. Reg. at 28041 (1976).
[6] 38 Fed. Reg. at 18720 (1973).

testify to the extent that he would be required to disclose, or to utilize his knowledge of, individual company data.

The second and third questions present related issues: (1) whether the QFR aggregate data meet tests of admissibility without inquiry into the underlying data, despite their arguably hearsay nature and respondent's right to "conduct such cross-examination as may be required for a full and true disclosure of the facts." 5 U.S.C. 556(d); and (2) whether the privilege against disclosure created by the QFR confidentiality rules is outweighed by respondent's need for individual company data.

Respondent relies on *Wirtz* v. *Baldor Elec. Co.,* 337 F.2d 518 (D.C. Cir. 1963) and *Powhatan Mining Co.* v. *Ickes,* 118 F.2d 105 (6th Cir. 1941), for the proposition that survey results may not be admitted into evidence unless the underlying data are made available to respondent's counsel. In both cases, the challenged survey results were tabulated specifically for use in administrative proceedings by officials who had exclusive access to the underlying material. The agency officials introduced the survey results into evidence during the administrative proceedings, but objected to discovery of the underlying survey data because of confidentiality provision. In neither case was the claim of privilege upheld.

The *Wirtz* and *Powhatan* cases may be distinguished on a number of grounds. First, while the Commission has followed the general rule making underlying data available when survey results are compiled for litigation, *Avnet, Inc.*, 78 F.T.C. 1562, 1563 n.1 (1971), there is no allegation here that tabulation of QFR data was in any way connected to this case. In fact, as the confidentiality rules make clear, QFR data are collected and reports prepared "for the purpose of preparing statistical compilations." 38 Fed. Reg. at 18720. Second, this is evidently not a case where a governmental party's introduction of survey results waives its right to a claim of privilege for underlying data to which it has access. See Wright & Miller, Federal Practice and Procedure: Civil Section 2019; *of. United States* v. *Reynolds,* 345 U.S. 1, 12 (1953). Rather, because of the strict confidentiality rules in effect, complaint counsel here have no access to the data General Foods is seeking; indeed, complaint counsel cannot produce the data because they have no authority to do so. *See United States* v. *International Business Mach. Corp.*, CCH 1975-2 Trade Cas. ¶ 60383, 66666-67 (S.D.N.Y. 1975). Third, should the preceding grounds for distinction not be deemed dispositive, the Commission notes that the *Wirtz* court held:

[D]ocuments supporting the tables and on which they are based must also be introduced or at least be made available to the opposing party *to the extent that they*

are necessary for purposes of rebuttal and cross-examination. 337 F.2d at 526. (Emphasis added.)

Thus, the respondent would be required to demonstrate why information on QFR methodology and procedures would be inadequate for rebuttal or cross-examination, and why individual company data are necessary.

It does not appear that the respondent has successfully made such a showing; and, as is discussed below, the record before the Commission is too limited to suggest whether or not this showing might be made in the future. The Commission will therefore not make a final determination on admissibility at this time, but will simply assume that the challenged QFR aggregate data may properly be introduced without necessarily requiring disclosure of individual company information.[7]

As to the issue of privilege, the Commission finds that the QFR rules create a qualified privilege for individual company data. This privilege is unique to government and may be termed a qualified confidential report privilege.[8] *See Association for Women in Science* v. *Califano*, 566 F.2d 339, 346 (D.C. Cir. 1977). This privilege requires a balancing of " 'the need of the litigants for information possessed by the Government and the need of the Government to foster the free flow of information provided to it' " recognizing that " 'clear and strong indication is required before it may be implied that the policy of prohibition is of such force as to dominate the broad objective of doing justice.' " *Id.* (citations omitted). *See Avnet, Inc.*, 77 F.T.C. 1686, 1687–88 (1970).

Respondent asserts a need for, and a basic procedural right to, unrestricted discovery of information as to the "validity, accuracy, reliability and composition" of QFR data for its "efforts to cross-

[7] Issues of admissibility are, in any event, best determined initially by the law judge. Rulings on the admissibility of the aggregate QFR data should be made, however, not only in light of the foregoing discussion, but also with regard to circumstantial guarantees of the trustworthiness of QFR reports and the necessity for using QFR data in aggregate form.

[8] As to the nature of the privilege created, the Commission recognizes that an absolute privilege against disclosure must be based on statutory language that at least specifically addresses the confidentiality of the material. The QFR confidentiality rules were based on Sections 6(f) and 6(g) of the FTC Act, 15 U.S.C.46(f), (g), and to some extent on confidentiality provisions of the Tax Reform Act of 1976, 23 U.S.C.6103, and prior tax law. While Section 6(f) does pertain specifically to confidential treatment of business information, it does not act as an absolute bar to the release of such data in adjudications. *See H.P. Hood & Sons, Inc.*, 58 F.T.C. 1148, 1150 (1961). Section 6(g) generally empowers the Commission to make rules and regulations for the purpose of carrying out the Act, and thus does not readily appear to support a claim of absolute privilege. The tax statutes deal explicitly with confidential treatment and may therefore provide the basis of an absolute privilege for some QFR material. In view of its disposition of this interlocutory appeal, the Commission need not decide the applicability of the tax statutes at this time, and will assume *arguendo* that they too support only a qualified privilege.

By contrast, the Commission's Line of Business confidentiality rules are based directly on statutory language that expressly protects LB data from disclosure. *See* 41 Fed. Reg. 28041, 34703 (1976); 40 Fed. Reg. 21542, 22318 (1975); Section 6 of the Federal Trade Commission Act, 15 U.S.C.46, as amended by Pub. Law No. 96–252; *see also* 88 Stat. 1822, 1840 (1974); 89 Stat. 611, 634 (1975), and 90 Stat. 937, 956 (1976). Such authority provides more compelling justification for a claim of absolute privilege. The type of evidentiary privilege that may be claimed for LB data is not at issue in this proceeding, however.

examine and defend against a benchmark based on that data, arguing that the aggregate data is not otherwise admissible." General Foods notes its prior objection to "utilization of QFR data for computing a 'competitive benchmark' and to receipt in evidence of documents containing the QFR calculations" and its prior questioning of complaint counsel's witness as to "the percentage of companies in the 'QFR benchmark' which are engaged in the sale of branded consumer grocery products and the number of food companies comprising the 'QFR benchmark'." (Memorandum of Respondent General Foods Corporation, at 1, 2, 3-4.) General Foods cites to statements assertedly casting doubt on the validity of QFR data and argues that the confidentiality rules were not intended to foreclose a respondent's inquiry under these circumstances. We need not decide the question of the admissibility of the aggregate QFR data at this time, but will assume it is admissible and discuss the application of the QFR rules to the individual company data.

Balanced against respondent's claims of need are complaint counsel's arguments that: (1) respondent has other means at its disposal sufficient to challenge use of QFR data; and (2) the "overriding concern" of the QFR rules to protect individual company data, and the evident purpose of the rules to encourage compliance with the reporting requirements by assuring confidentiality. The parties have referred to such matters as the reliability of the QFR data, the adequacy of the information respondent has already obtained, and the degree to which the QFR data are relied on exclusively in this case. However, a full record is not before the Commission on these and other issues concerning the respondent's need for the data, nor should it be at this stage.

Rather, it is within the broad discretion of the ALJ to rule on discovery and evidentiary questions, including privilege, in light of the circumstances of the proceeding. *Missouri Portland Cement Co.*, 77 F.T.C. 1688, 1689-70 (1970). The purpose of Rule 3.36 (concerning subpoenas addressed to the Commission or its employees) may be understood in light of a predecessor provision, which required certification to the full Commission of requests for subpoenas to government officials. There, the Commission said that the purpose of the rule "is not to relieve the examiner of his essential role" concerning basic questions of discovery and evidence, but rather "to provide a means of informing the Commission of any such action to prevent the possibility of abuse" and to "give the Commission an opportunity to work out appropriate arrangements with other agencies involved if a request is found to be justified." *Avnet, Inc.*, *supra*, 77 F.T.C. at 1687-88, 1688 n.3. Here, although it is not obvious

from the papers before the Commission that inquiry into individual company data was contemplated by the ALJ in issuing the subpoena, and, if so, how he viewed the confidentiality rules, the Commission must make an interim decision on the scope of discovery, reserving to the ALJ (and to the Commission on review of the entire record of the proceeding) the ultimate resolution of this issue.

Based on the necessarily limited record, the Commission has determined that the agency's need for accurate, timely and complete individual company QFR data (including company names) is more compelling than respondent's need for that data. *See Association for Women in Science* v. *Califano*, *supra*, 566 F.2d at 346–47.[9] Nor is respondent's need so evident from the materials before the Commission to require disclosure under a protective order. Therefore, the Commission will at this time construe the QFR confidentiality rules to create a qualified privilege, barring the testimony of Mr. Sprunk as to individual company data in connection with the QFR program.

Accordingly, *it is ordered,* That William H. Sprunk may, consistent with the Commission's LB and QFR confidentiality rules, appear and testify in response to the Administrative Law Judge's subpoena *ad testificandum* issued March 3, 1980, but that the inquiry be limited to only those questions which would not disclose "the names of companies, financial data, and all other information which are obtained from the respondent companies" as protected by the QFR confidentiality rules in connection with the QFR program. The General Counsel is directed to represent Mr. Sprunk for the purpose of asserting any other privileges arising out of his Commission employment.

Commissioner Bailey did not participate.

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[9] This conclusion is based, in part, on the nature of respondent's QFR criticisms. These criticisms relate to the methodology and procedures for compiling the QFR reports, aspects of the QFR program into which respondent can inquire of Mr. Sprunk without inquiring into individual company data. See *Avnet, Inc.*, *supra*, 78 F.T.C. at 1563.

Moreover, given the agency's compelling need to obtain the QFR data, respondent must make a strong showing of need in order to overcome the qualified privilege and thereby compel disclosure of the individual company information. On the record as it now stands, respondent's showing is wholly inadequate.

IN THE MATTER OF

GENERAL FOODS CORPORATION

Docket 9085. Interlocutory Order, Aug. 19, 1980

ORDER ON FOLGER'S APPLICATION FOR REVIEW

The Folger Coffee Company and the Procter & Gamble Company (hereinafter collectively referred to as "Folger") have applied to the Commission for review of the Administrative Law Judge's order of April 9, 1980, denying continued *in camera* treatment of certain exhibits and related testimony. The law judge has certified Folger's appeal to the Commission pursuant to Rule 3.23(b). Complaint counsel have filed an answer opposing this appeal.

The exhibits in question consist primarily of Folger memoranda, written during the period of 1971 to mid-1976, concerning the company's then ongoing expansion into the markets of the eastern states. The law judge found that these documents analyzed the new markets, discussed the strengths and weaknesses of both Folger and its competitors, and described Folger's promotional activity, such as its use of advertising, discount coupons, and pricing allowances. These and other exhibits for which *in camera* treatment is sought also contain detailed information on Folger's sales, costs, revenues, and profits nationally and in specific areas. Finally, Folger asks that *in camera* status be given to testimony on these exhibits as well as to testimony on the results of a taste test comparing Maxwell House and Folger coffees and on the impact of a 1975 frost in Brazil.

The law judge concluded that the release of most of the exhibits and testimony covered by Folger's request would not be likely to result in "clearly defined, serious injury," as set forth in *H.P. Hood & Sons, Inc.*, 58 F.T.C. 1148 (1961). He therefore denied Folger's motion, subject to only two exceptions. First, he granted *in camera* treatment for testimony on Folger's northeast expansion, which he found would be of present value to competitors since Folger's expansion there is still underway. Second, he determined to retain *in camera* treatment of testimony and an excerpt from an exhibit (RX 1080) that disclosed Folger's profits on High Point coffee for the years 1976 through 1979. The High Point data were deemed particularly sensitive because the product is still being test marketed.

Folgers presents four arguments in support of its *in camera* request. First, in its motion before the law judge, Folger has contended that the information in the exhibits and testimony in question is secret and material to its business, and, taken as a whole, constitutes a "unique encyclopedia of marketing knowledge." Folger

insists that, regardless of their age, these materials would be valuable to competitors by affording them the benefits of Folger's experiences in entering new markets and by disclosing to them Folger's strategies for mounting or responding to competitive challenges. Second, in its application for review, the company states that the 1976–1979 profit data on High Point coffee appears in an exhibit containing similar data on Folger vacuum and flaked coffee, and argues that these recent data are equally sensitive and equally deserving of *in camera* protection. Third, Folger points out that it is not a party to this proceeding and asserts that it should not have to make the same kinds of showings for *in camera* treatment as parties are required to present. Fourth, in a memorandum supplementing its application for review,[1] the company contends that amendments to the Commission's statute made by the Federal Trade Commission Improvements Act of 1980, Pub. Law No. 96–252, prohibit the Commission from removing any of the materials at issue here from *in camera* status.

The last two arguments can be disposed of quickly. Concerning the effect of the amendatory legislation, we agree with Folger that Section 6(f) of the Federal Trade Commission Act now secures confidential treatment for a broader class of business information obtained by the Commission. However, we do not agree that anything in the Federal Trade Commission Improvements Act, or its legislative history, weakens the long-held position that Section 6(f) does not absolutely bar disclosure of business data as evidence in adjudicatory proceedings. *See H.P. Hood & Sons, Inc.* New Section 21(d)(2) of the FTC Act provides that "[a]ny disclosure of relevant and material information in adjudicative proceedings to which the Commission is a party shall be governed by the rules of the Commission for adjudicative proceedings . . . except that the rules of the Commission shall not be amended in a manner inconsistent with the purposes of this section." Discussing what ultimately was enacted as Section 21(d)(2), the Senate Report on S.1991 stated specifically that the Commission should maintain the procedures in Rules 1.18(b) and 3.45 for granting *in camera* treatment. Senate Report No. 96–500 at pp. 27–28 (1979). Rule 3.45 governs Folger's instant request, and provides that evidence may be held *in camera* only for good cause, citing *H.P. Hood & Sons, Inc.* as support. Thus, the recent amendments to the Federal Trade Commission Act only support the view that Section 6(f)'s confidentiality provisions do not prohibit disclosure of evidence in adjudications.

[1] Folger's request to file its supplementary memorandum of June 26, 1980, is hereby granted.

As to Folger's contention that third parties should be afforded more lenient standards for *in camera* treatment, we similarly note that such a rule would conflict with consistent Commission policy. While it is true that in *Crown Cork & Seal Co.*, 71 F.T.C. 1714 (1967), we suggested that the *in camera* request of an uninvolved bystander warranted special solicitude, we nevertheless applied the same standards as had been enunciated in *H.P. Hood & Sons, Inc.*, and denied *in camera* treatment. Furthermore, our decision in *Bristol-Myers Co.*, 90 F.T.C. 455 (1977), which elaborated on the *Hood* standards, also involved an *in camera* request from a non-respondent.

Folger's remaining two arguments present no new questions of law or policy, but simply raise the issue whether the law judge has properly applied the Commission's guidelines for *in camera* status to the facts before him. In our order of March 10, 1980, concerning General Food's own *in camera* motion, we stated that the bases for *in camera* treatment were secrecy and materiality, and advised law judges to consider the six factors listed in the Restatement of Torts citing our *Bristol-Myers* opinion. We also stated that "administrative law judges have broad discretion in determining what information should be placed *in camera* and we do not ordinarily disturb their determinations except on the basis of showing of abuse," Order of March 10, 1980 at p.3. We emphasize that point here. If the law judge has properly interpreted the Commission's *in camera* standards and applied them clearly to the facts in issue, we will be reluctant to question his conclusions. At the interlocutory stage, we are neither familiar with the broad contours of the case below or the specifics of the information in question, and we are therefore ill-equipped to second-guess an ALJ's factual findings on *in camera* motions.

In the present case, we are not prepared to overturn the law judge's decision to deny *in camera* treatment to most of the exhibits and testimony covered by Folger's motion. The law judge carefully reviewed Folger's arguments concerning each of the six factors cited in our *Bristol-Myers* order, and concluded that the information in question may at one time have provided competitors with advantages had it been released. However, the ALJ also noted that the documents were three and a half to nine years old, and dealt with marketing campaigns that have already been put into effect. He concluded, therefore, that Folger's competitors have already obtained, through experience, much of the business information contained in the exhibits and testimony and that their release now would not be likely to result in serious injury. While there may be some merit in Folger's argument that discussions of its marketing

and promotional strategies might continue to have significance to competitors, we have previously placed movants for *in camera* treatment under a greater burden when the information is old. *See, e.g., General Foods*, Docket No. 9085, Order of March 10, 1980; *Crown Cork & Seal Co., supra.* That is the case here, and we do not believe we are in a position to question the law judge's specific finding that the information at issue has not lost its competitive sensitivity.

In contrast, the law judge has not clearly articulated his reason for distinguishing between recent profit data on High Point coffee and profit and sales data on Folger's vacuum and flaked coffees. Presumably, he may have concluded that the release of such data on the vacuum and flaked brands would not seriously injure Folger since they already have established market positions. However, as we note in our companion order on General Foods' *in camera* motion, the law judge may have construed the meaning of the "clearly defined, serious injury standard" too narrowly, so as to require a specific demonstration of how the release of concededly secret and material information would be likely to injure the competitor that provided it.[2] Given this possibility, coupled with the apparent sensitivity of recent coffee profit data, we believe that the law judge should provide a more explicit analysis of why the release of such data is not likely to prove harmful. Accordingly, we remand on the narrow issue of whether the remainder of RX 1080 and any testimony thereon should be held *in camera*.[3] We reiterate, however, that once the law judge reconsiders this issue and articulates his position under the appropriate standards,[4] his determination will be upheld absent an abuse of discretion. Accordingly,

It is ordered, That Folger's application is denied except to the extent that it seeks in camera treatment for the entirety of RX 1080 and testimony thereon, in which respect it is remanded for reconsideration and additional findings.

Commissioner Bailey did not participate.

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[2] Order Denying in Part and Remanding in Part General Foods' Application for Review at p. 2.

[3] As we stated in our order of March 10, particularly difficult questions may be resolved by granting *in camera* status to information until the close of trial, at which point the law judge may review the motion, or until appeal to the Commission which may take up the motion when it has greater familiarity with the case and access to the information itself.

[4] Recent sales and profit data generally suggest themselves as being both secret and material to the firm concerned. Specific inquiries relevant to the secrecy and materiality of such data include whether substantially equivalent information is available from other sources and, if not, whether the products concerned are so well established in the market that disclosures about them would not prove injurious. In addition, as we state in our order today concerning General Foods' own *in camera* request, "when certain information is found to be materially valuable and secret to a firm's competitive business activities, the Administrative Law Judge may infer, without a specific showing of how a competitor would use it, that the loss of information would adversely affect the possessor's commercial position." Order Denying in Part and Remanding in Part General Foods' Application for Review at p. 2.

IN THE MATTER OF

MIDLAND-ROSS CORPORATION

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT AND SEC. 8 OF THE CLAYTON ACT

Docket C-3035. Complaint, Aug. 21, 1980—Decision, Aug. 21, 1980

This consent order prohibits, among other things, a Cleveland, Ohio corporation from having as a director any individual who also serves as a director of a competitive company whose revenues exceed the lesser of ten million dollars, or one percent of the company's total annual revenues.

Appearances

For the Commission: *Dennis F. Johnson* and *Thomas J. Keary.*

For the respondent: *Robert H. Rawson, Jr., Jones, Day, Reavis & Pogue,* Cleveland, Ohio.

COMPLAINT

The Federal Trade Commission, having reason to believe that the above-named respondents have violated the provisions of Section 8 of the Clayton Act, 15 U.S.C. 19, and Section 5(a)(1) of the Federal Trade Commission Act, 15 U.S.C. 45(a)(1), and that a proceeding by it in respect thereof would be in the public interest, issues this complaint, stating its charges as follows:

COUNT I

PARAGRAPH 1. Gould Inc. ("Gould") is a corporation organized under the laws of the State of Delaware, with its principal place of business located at 10 Gould Center, Rolling Meadows, Illinois. Gould has capital, surplus and undivided profits aggregating more than one million dollars.

PAR. 2. Respondent Midland-Ross Corporation ("Midland-Ross") is a corporation organized under the laws of the State of Ohio, with its principal place of business located at 20600 Chagrin Boulevard, Cleveland, Ohio. Midland-Ross has capital, surplus and undivided profits aggregating more than one million dollars.

PAR. 3. Respondent Claude M. Blair is an individual, with his principal place of business located at National City Corporation, Post Office Box 5756, Cleveland, Ohio.

PAR. 4. Gould conducts its business, as described herein, in various

States of the United States and is thereby engaged in activity in or affecting commerce within the meaning of Section Four of the Federal Trade Commission Act, as amended, 15 U.S.C. 44, and Section 1 of the Clayton Act, 15 U.S.C. 12.

PAR. 5. Midland-Ross conducts its business, as described herein, in various States of the United States and is thereby engaged in activity in or affecting commerce within the meaning of Section Four of the Federal Trade Commission Act, as amended, 15 U.S.C. 44, and Section 1 of the Clayton Act, 15 U.S.C. 12.

PAR. 6. Claude M. Blair was, until his resignation from Gould's board of directors on or about July 24, 1979, a member of the boards of directors of both Gould and Midland-Ross. He has been a director of Midland-Ross since 1974, and was a director of Gould from 1969 until his resignation.

PAR. 7. During all or part of the period that Claude M. Blair concurrently served as a director of Gould and Midland-Ross, the business of Gould and Midland-Ross included the manufacture and sale of various electrical products, including electrical busways and electrical conduit fittings.

PAR. 8. By the nature of their business as hereinabove described and the locations of their operations, Gould and Midland-Ross have been competitors, during all or part of the time period that Claude M. Blair concurrently served as a director of Gould and Midland-Ross, so that the elimination of competition by agreement between them would constitute a violation of the antitrust laws.

PAR. 9. The simultaneous membership of Claude M. Blair on the boards of directors of Gould and Midland-Ross constitutes a violation of Section 8 of the Clayton Act and Section 5(a)(1) of the Federal Trade Commission Act.

COUNT II

PAR. 10. Paragraphs One and Four are incorporated herein.

PAR. 11. Respondent Narco Scientific, Inc. ("Narco") is a corporation organized under the laws of the State of Delaware, with its principal place of business located at Fort Washington Industrial Park, Fort Washington, Pennsylvania. Narco has capital, surplus and undivided profits aggregating more than one million dollars.

PAR. 12. Respondent William C. Musham is an individual, with his principal place of business located at Gould Inc., 10 Gould Center, Rolling Meadows, Illinois.

PAR. 13. Narco conducts its business, as described herein, in various States of the United States and is thereby engaged in activity

in or affecting commerce within the meaning of Section Four of the Federal Trade Commission Act, as amended, 15 U.S.C. 44, and Section 1 of the Clayton Act, 15 U.S.C. 12.

PAR. 14. William C. Musham was, until his resignation from Narco's board of directors during January 1980, a member of the boards of directors of both Gould and Narco. He has been a director of Gould since 1976, and was a director of Narco from 1977 until his resignation.

PAR. 15. During all or part of the period that William C. Musham concurrently served as a director of Gould and Narco, the business of Gould and Narco included the manufacture and sale of electronic medical devices.

PAR. 16. By the nature of their business as hereinabove described and the locations of their operations, Gould and Narco have been competitors, during all or part of the time period that William C. Musham concurrently served as a director of Gould and Narco, so that the elimination of competition by agreement between them would constitute a violation of the antitrust laws.

PAR. 17. The simultaneous membership of William C. Musham on the boards of directors of Gould and Narco constitutes a violation of Section 8 of the Clayton Act and Section 5(a)(1) of the Federal Trade Commission Act.

DECISION AND ORDER

The Federal Trade Commission, having initiated an investigation of interlocking personnel relationships between Gould Inc. and other corporations, and Midland-Ross Corporation (hereinafter referred to as "Midland-Ross"), having been furnished thereafter with a copy of a draft of complaint which the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge Midland-Ross with violation of Section 8 of the Clayton Act (15 U.S.C. 19) and Section 5 of the Federal Trade Commission Act (15 U.S.C. 45); and

Midland-Ross, its attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by Midland-Ross of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by Midland-Ross that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and

having determined that it had reason to believe that Midland-Ross has violated the said Acts, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Midland-Ross is a corporation organized, existing and doing business under and by virtue of the laws of the State of Ohio, with its office and principal place of business located at 20600 Chagrin Boulevard, Cleveland, Ohio.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of Midland-Ross, and the proceeding is in the public interest.

ORDER

I

It is ordered, That the following definitions shall apply herein:

(a) "Subsidiary" of a corporation means any corporation, partnership, firm, association or other legal or business entity of which 50 percent or more of the issued and outstanding voting securities (or other indicia of control for non-stock business organizations) is owned or controlled, directly or indirectly, by such corporation.

(b) "Parent" means any corporation which owns or controls 50 percent or more of the issued and outstanding voting securities (or other indicia of control for non-stock business organizations) of any other business organization.

(c) "Sister" corporations mean corporations that share a common parent.

(d) "Product or service market" means any line of commerce in which Midland-Ross' (including its subsidiaries and divisions) annual revenues exceed the lesser of:

(1) five million dollars; or
(2) one-half of one percent of Midland-Ross' total annual revenues.

II

It is further ordered, That Midland-Ross, its subsidiaries, successors and assigns, shall forthwith cease and desist from having, and in the future shall not have, any director who also serves as a director

of any other corporation if Midland-Ross and such other corporation are, by virtue of their business and location of operation, competitors, so that the elimination of competition between them would constitute a violation of any of the antitrust laws, providing that the revenues of either corporation derived from the product or service market(s) in which they are competitors exceed the lesser of:

(a) Ten million dollars; or
(b) One percent of the total annual revenues of that corporation.

III

It is further ordered, That within thirty (30) days of the date of service of this order, and annually thereafter, Midland-Ross shall obtain, review, and retain from and as to each of its directors, the name and address of each other corporation not related to Midland-Ross as parent, sister or subsidiary, which such director also serves as a director, and a descriptive listing of all products and services manufactured, produced, sold or leased by each such other corporation. Midland-Ross shall not permit any person to serve as a director who fails to submit to Midland-Ross any information required by this paragraph. Midland-Ross shall provide the information received pursuant to this paragraph to the Commission upon request. If competition arises in any product or service market between Midland-Ross and any other corporation with which Midland-Ross shares a common director, by virtue of action taken by such other corporation subsequent to a submission of information by such director pursuant to this paragraph, then Midland-Ross shall not be liable under Paragraph II until the date for the next submission of information.

IV

It is further ordered, That within ten (10) days from the date of issuance of this order Midland-Ross shall distribute a copy of this order to each of its current directors and thereafter, shall distribute a copy of this order to each prospective or newly-elected or appointed director.

V

It is further ordered, That Midland-Ross shall:

(a) within sixty (60) days after the date of service of this order, file

with the Commission a written report setting forth in detail the manner and form in which it has complied with this order; and

(b) file with the Commission such other reports of compliance as may be requested by the Commission.

VI

It is further ordered, That the obligations imposed upon Midland-Ross under the terms of this order shall continue for a period of seven years following the date of service of this order.

VII

It is further ordered, That Midland-Ross shall notify the Commission not more than thirty (30) days after any change in the corporation such as dissolution, assignment, or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries, or any other change in the corporation which may affect compliance obligations arising out of this order.

IN THE MATTER OF

NARCO SCIENTIFIC, INC.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT AND SEC. 8 OF THE CLAYTON ACT

Docket C-3036. Complaint, Aug. 21, 1980—Decision, Aug. 21, 1980

This consent order prohibits, among other things, a Fort Washington, Pa. corporation from having as a director any individual who also serves as a director of any competitive company whose revenues exceed the lesser of ten million dollars or one percent of the company's total annual revenues.

Appearances

For the Commission: *Dennis F. Johnson* and *Thomas J. Keary.*

For the respondent: *James G. Rosenberg, Saul, Ewing, Remick & Saul,* Philadelphia, Pa.

COMPLAINT

The Federal Trade Commission, having reason to believe that the above-named respondents have violated the provisions of Section 8 of the Clayton Act, 15 U.S.C. 19, and Section 5(a)(1) of the Federal Trade Commission Act, 15 U.S.C. 45(a)(1), and that a proceeding by it in respect thereof would be in the public interest, issues this complaint, stating its charges as follows:

COUNT I

PARAGRAPH 1. Gould Inc. ("Gould") is a corporation organized under the laws of the State of Delaware, with its principal place of business located at 10 Gould Center, Rolling Meadows, Illinois. Gould has capital, surplus and undivided profits aggregating more than one million dollars.

PAR. 2. Respondent Midland-Ross Corporation ("Midland-Ross") is a corporation organized under the laws of the State of Ohio, with its principal place of business located at 20600 Chagrin Boulevard, Cleveland, Ohio. Midland-Ross has capital, surplus and undivided profits aggregating more than one million dollars.

PAR. 3. Respondent Claude M. Blair is an individual, with his principal place of business located at National City Corporation, Post Office Box 5756, Cleveland, Ohio.

PAR. 4. Gould conducts its business, as described herein, in various

States of the United States and is thereby engaged in activity in or affecting commerce within the meaning of Section Four of the Federal Trade Commission Act, as amended, 15 U.S.C. 44, and Section 1 of the Clayton Act, 15 U.S.C. 12.

PAR. 5. Midland-Ross conducts its business, as described herein, in various States of the United States and is thereby engaged in activity in or affecting commerce within the meaning of Section Four of the Federal Trade Commission Act, as amended, 15 U.S.C. 44, and Section 1 of the Clayton Act, 15 U.S.C. 12.

PAR. 6. Claude M. Blair was, until his resignation from Gould's board of directors on or about July 24, 1979, a member of the boards of directors of both Gould and Midland-Ross. He has been a director of Midland-Ross since 1974, and was a director of Gould from 1969 until his resignation.

PAR. 7. During all or part of the period that Claude M. Blair concurrently served as a director of Gould and Midland-Ross, the business of Gould and Midland-Ross included the manufacture and sale of various electrical products, including electrical busways and electrical conduit fittings.

PAR. 8. By the nature of their business as hereinabove described and the locations of their operations, Gould and Midland-Ross have been competitors, during all or part of the time period that Claude M. Blair concurrently served as a director of Gould and Midland-Ross, so that the elimination of competition by agreement between them would constitute a violation of the antitrust laws.

PAR. 9. The simultaneous membership of Claude M. Blair on the boards of directors of Gould and Midland-Ross constitutes a violation of Section 8 of the Clayton Act and Section 5(a)(1) of the Federal Trade Commission Act.

COUNT II

PAR. 10. Paragraphs One and Four are incorporated herein.

PAR. 11. Respondent Narco Scientific, Inc. ("Narco") is a corporation organized under the laws of the State of Delaware, with its principal place of business located at Fort Washington Industrial Park, Fort Washington, Pennsylvania. Narco has capital, surplus and undivided profits aggregating more than one million dollars.

PAR. 12. Respondent William C. Musham is an individual, with his principal place of business located at Gould Inc., 10 Gould Center, Rolling Meadows, Illinois.

PAR. 13. Narco conducts its business, as described herein, in various States of the United States and is thereby engaged in activity

in or affecting commerce within the meaning of Section Four of the Federal Trade Commission Act, as amended, 15 U.S.C. 44, and Section 1 of the Clayton Act, 15 U.S.C. 12.

PAR. 14. William C. Musham was, until his resignation from Narco's board of directors during January 1980, a member of the boards of directors of both Gould and Narco. He has been a director of Gould since 1976, and was a director of Narco from 1977 until his resignation.

PAR. 15. During all or part of the period that William C. Musham concurrently served as a director of Gould and Narco, the business of Gould and Narco included the manufacture and sale of electronic medical devices.

PAR. 16. By the nature of their business as hereinabove described and the locations of their operations, Gould and Narco have been competitors, during all or part of the time period that William C. Musham concurrently served as a director of Gould and Narco, so that the elimination of competition by agreement between them would constitute a violation of the antitrust laws.

PAR. 17. The simultaneous membership of William C. Musham on the boards of directors of Gould and Narco constitutes a violation of Section 8 of the Clayton Act and Section 5(a)(1) of the Federal Trade Commission Act.

DECISION AND ORDER

The Federal Trade Commission, having initiated an investigation of interlocking personnel relationships between Gould Inc. and other corporations, and Narco Scientific, Inc. (hereinafter referred to as "Narco"), having been furnished thereafter with a copy of a draft of complaint which the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge Narco with violation of Section 8 of the Clayton Act (15 U.S.C. 19) and Section 5 of the Federal Trade Commission Act (15 U.S.C. 45); and

Narco, its attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by Narco of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by Narco that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and

having determined that it had reason to believe that Narco has violated the said Acts, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Narco is a corporation organized existing and doing business under and by virtue of the laws of the State of Delaware, with its office and principal place of business located at Fort Washington Industrial Park, Fort Washington, Pennsylvania.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of Narco, and the proceeding is in the public interest.

ORDER

I

It is ordered, That the following definitions shall apply herein:

(a) "Subsidiary" of a corporation means any corporation, partnership, firm, association or other legal or business entity of which 50 percent or more of the issued and outstanding voting securities (or other indicia of control for non-stock business organizations) is owned or controlled, directly or indirectly, by such corporation.

(b) "Parent" means any corporation which owns or controls 50 percent or more of the issued and outstanding voting securities (or other indicia of control for non-stock business organizations) of any other business organization.

(c) "Sister" corporations mean corporations that share a common parent.

(d) "Product or service market" means any line of commerce in which Narco's (including its subsidiaries and divisions) annual revenues exceed the lesser of:

(1) Five million dollars; or

(2) One-half of one percent of Narco's total annual revenues.

II

It is further ordered, That Narco, its subsidiaries, successors and assigns, shall forthwith cease and desist from having, and in the future shall not have, any director who also serves as a director of

any other corporation if Narco and such other corporation are, by virtue of their business and location of operation, competitors, so that the elimination of competition between them would constitute a violation of any of the antitrust laws, providing that the revenues of either corporation derived from the product or service market(s) in which they are competitors exceed the lesser of:

(a) Ten million dollars; or
(b) One percent of the total sales of that corporation.

III

It is further ordered, That within thirty (30) days of the date of service of this order, and annually thereafter, Narco shall obtain, review, and retain from and as to each of its directors, the name and address of each other corporation not related to Narco as parent, sister or subsidiary, which such director also serves as a director, and a descriptive listing of all products and services manufactured, produced, sold or leased by each such other corporation. Narco shall not permit any person to serve as a director who fails to submit to Narco any information required by this paragraph. Narco shall provide the information received pursuant to this paragraph to the Commission upon request. If competition arises in any product or service market between Narco and any other corporation with which Narco shares a common director, by virtue of action taken by such other corporation subsequent to a submission of information by such director pursuant to this paragraph, then Narco shall not be liable under Paragraph II until the date for the next submission of information.

IV

It is further ordered, That within ten (10) days from the date of issuance of this order Narco shall distribute a copy of this order to each of its current directors, and thereafter, shall distribute a copy of this order to each prospective or newly-elected or appointed director.

V

It is further ordered, That Narco shall:

(a) within sixty (60) days after the date of service of this order, file with the Commission a written report setting forth in detail the manner and form in which it has complied with this order; and

(b) file with the Commission such other reports of compliance as may be requested by the Commission.

VI

It is further ordered, That the obligations imposed upon Narco under the terms of this order shall continue for a period of seven years following the date of service of this order.

VII

It is further ordered, That Narco shall notify the Commission not more than thirty (30) days after any change in the corporation such as dissolution, assignment, or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries, or any other change in the corporation which may affect compliance obligations arising out of this order.

IN THE MATTER OF

CLAUDE M. BLAIR

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT AND SEC. 8 OF THE CLAYTON ACT

Docket C-3037. Complaint, Aug. 21, 1980—Decision, Aug. 21, 1980

This consent order prohibits, among other things, an individual whose principal place of business is located at the National City Corporation in Cleveland, Ohio, from serving simultaneously as a director of two or more competing companies, any one of which has capital, surplus, and undivided profits aggregating more than one million dollars and revenues that exceed the lesser of ten million dollars, or one percent of the corporation's total revenues.

Appearances

For the Commission: *Dennis F. Johnson* and *Thomas J. Keary.*

For the respondent: *Robert H. Rawson, Jr., Jones, Day, Reavis & Pogus*, Cleveland, Ohio.

COMPLAINT

The Federal Trade Commission, having reason to believe that the above-named respondents have violated the provisions of Section 8 of the Clayton Act, 15 U.S.C. 19, and Section 5(a)(1) of the Federal Trade Commission Act, 15 U.S.C. 45(a)(1), and that a proceeding by it in respect thereof would be in the public interest, issues this complaint, stating its charges as follows:

COUNT I

PARAGRAPH 1. Gould Inc. ("Gould") is a corporation organized under the laws of the State of Delaware, with its principal place of business located at 10 Gould Center, Rolling Meadows, Illinois. Gould has capital, surplus and undivided profits aggregating more than one million dollars.

PAR. 2. Respondent Midland-Ross Corporation ("Midland-Ross") is a corporation organized under the laws of the State of Ohio, with its principal place of business located at 20600 Chagrin Boulevard, Cleveland, Ohio. Midland-Ross has capital, surplus and undivided profits aggregating more than one million dollars.

PAR. 3. Respondent Claude M. Blair is an individual, with his

principal place of business located at National City Corporation, Post Office Box 5756, Cleveland, Ohio.

PAR. 4. Gould conducts its business, as described herein, in various States of the United States and is thereby engaged in activity in or affecting commerce within the meaning of Section Four of the Federal Trade Commission Act, as amended, 15 U.S.C. 44, and Section 1 of the Clayton Act, 15 U.S.C. 12.

PAR. 5. Midland-Ross conducts its business, as described herein, in various States of the United States and is thereby engaged in activity in or affecting commerce within the meaning of Section Four of the Federal Trade Commission Act, as amended, 15 U.S.C. 44, and Section 1 of the Clayton Act, 15 U.S.C. 12.

PAR. 6. Claude M. Blair was, until his resignation from Gould's board of directors on or about July 24, 1979, a member of the boards of directors of both Gould and Midland-Ross. He has been a director of Midland-Ross since 1974, and was a director of Gould from 1969 until his resignation.

PAR. 7. During all or part of the period that Claude M. Blair concurrently served as a director of Gould and Midland-Ross, the business of Gould and Midland-Ross included the manufacture and sale of various electrical products, including electrical busways and electrical conduit fittings.

PAR. 8. By the nature of their business as hereinabove described and the locations of their operations, Gould and Midland-Ross have been competitors, during all or part of the time period that Claude M. Blair concurrently served as a director of Gould and Midland-Ross, so that the elimination of competition by agreement between them would constitute a violation of the antitrust laws.

PAR. 9. The simultaneous membership of Claude M. Blair on the boards of directors of Gould and Midland-Ross consititutes a violation of Section 8 of the Clayton Act and Section 5(a)(1) of the Federal Trade Commission Act.

COUNT II

PAR. 10. Paragraphs One and Four are incorporated herein.

PAR. 11. Respondent Narco Scientific, Inc. ("Narco") is a corporation organized under the laws of the State of Delaware, with its principal place of business located at Fort Washington Industrial Park, Fort Washington, Pennsylvania. Narco has capital, surplus and undivided profits aggregating more than one million dollars.

PAR. 12. Respondent William C. Musham is an individual, with his

principal place of business located at Gould Inc., 10 Gould Center, Rolling Meadows, Illinois.

PAR. 13. Narco conducts its business, as described herein, in various States of the United States and is thereby engaged in activity in or affecting commerce within the meaning of Section Four of the Federal Trade Commission Act, as amended, 15 U.S.C. 44, and Section 1 of the Clayton Act, 15 U.S.C. 12.

PAR. 14. William C. Musham was, until his resignation from Narco's board of directors during January 1980, a member of the boards of directors of both Gould and Narco. He has been a director of Gould since 1976, and was a director of Narco from 1977 until his resignation.

PAR. 15. During all or part of the period that William C. Musham concurrently served as a director of Gould and Narco, the business of Gould and Narco included the manufacture and sale of electronic medical devices.

PAR. 16. By the nature of their business as hereinabove described and the locations of their operations, Gould and Narco have been competitors, during all or part of the time period that William C. Musham concurrently served as a director of Gould and Narco, so that the elimination of competition by agreement between them would constitute a violation of the antitrust laws.

PAR. 17. The simultaneous membership of William C. Musham on the boards of directors of Gould and Narco constitutes a violation of Section 8 of the Clayton Act and Section 5(a)(1) of the Federal Trade Commission Act.

DECISION AND ORDER

The Federal Trade Commission, having initiated an investigation of interlocking personnel relationships between Gould Inc. and other corporations, and Claude M. Blair, having been furnished thereafter with a copy of a draft of complaint which the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge Claude M. Blair with violation of Section 8 of the Clayton Act (15 U.S.C. 19) and Section 5 of the Federal Trade Commission Act (15 U.S.C. 45); and

Claude M. Blair, his attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by Claude M. Blair of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by Claude M. Blair that the law has been

violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that Claude M. Blair has violated the said Acts, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Claude M. Blair is an individual with his office and principal place of business located at National City Corporation, P.O. Box 5756, Cleveland, Ohio.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of Claude M. Blair, and the proceeding is in the public interest.

ORDER

I

It is ordered, That the following definition shall apply herein:

"Product or service market" means any line of commerce in which the annual revenues of a corporation of which Claude M. Blair is a director exceed the lesser of:

(a) Five million dollars; or

(b) One-half of one percent of the total annual revenues of that corporation.

II

It is further ordered, That Claude M. Blair shall not be a director in any two or more corporations, any one of which has capital, assets, and undivided profits aggregating more than one million dollars, engaged in whole or in part in commerce, if such corporations are, by virtue of their business and location of operation, competitors, so that the elimination of competition by agreement between them would constitute a violation of any of the provisions of any of the antitrust laws, providing that the revenues of either corporation derived from the product or service market(s) in which they are competitors exceed the lesser of:

(a) Ten million dollars; or

(b) One percent of the total revenues of that corporation.

If, after his election, competition arises in any product or service market between corporations upon which Claude M. Blair serves as a director such as would cause him to violate the terms of this paragraph, then Claude M. Blair shall not be liable under this paragraph until the date of the first annual meeting of shareholders following the time such competition arose.

III

It is further ordered, That Claude M. Blair shall:

(a) within sixty (60) days after the date of service of this order, file with the Commission a written report setting forth in detail the manner and form in which he has complied with this order; and

(b) file with the Commission such other reports of compliance as may be requested by the Commission.

IV

It is further ordered, That the obligations imposed upon Claude M. Blair under the terms of this order shall continue for a period of five years following the date of service of this order.

IN THE MATTER OF

WILLIAM C. MUSHAM

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT AND SEC. 8 OF THE CLAYTON ACT

Docket C-3038. Complaint, Aug. 21, 1980—Decision, Aug. 21, 1980

This consent order prohibits, among other things, an individual whose principal place of business is located at Gould, Inc. in Rolling Meadows, Ill. from serving simultaneously as a director of two or more competing companies, any one of which has capital, surplus, and undivided profits aggregating more than one million dollars; and revenues that exceed the lesser of ten million dollars or one percent of the corporation's total revenues.

Appearances

For the Commission: *Dennis F. Johnson* and *Thomas J. Keary.*

For the respondent: *Edward M. Posner, Drinker, Biddle & Reath,* Philadelphia, Pa.

COMPLAINT

The Federal Trade Commission, having reason to believe that the above-named respondents have violated the provisions of Section 8 of the Clayton Act, 15 U.S.C. 19, and Section 5(a)(1) of the Federal Trade Commission Act, 15 U.S.C. 45(a)(1), and that a proceeding by it in respect thereof would be in the public interest, issues this complaint, stating its charges as follows:

COUNT I

PARAGRAPH 1. Gould Inc. ("Gould") is a corporation organized under the laws of the State of Delaware, with its principal place of business located at 10 Gould Center, Rolling Meadows, Illinois. Gould has capital, surplus and undivided profits aggregating more than one million dollars.

PAR. 2. Respondent Midland-Ross Corporation ("Midland-Ross") is a corporation organized under the laws of the State of Ohio, with its principal place of business located at 20600 Chagrin Boulevard, Cleveland, Ohio. Midland-Ross has capital, surplus and undivided profits aggregating more than one million dollars.

PAR. 3. Respondent Claude M. Blair is an individual, with his

principal place of business located at National City Corporation, Post Office Box 5756, Cleveland, Ohio.

PAR. 4. Gould conducts its business, as described herein, in various States of the United States and is thereby engaged in activity in or affecting commerce within the meaning of Section Four of the Federal Trade Commission Act, as amended, 15 U.S.C. 44, and Section 1 of the Clayton Act, 15 U.S.C. 12.

PAR. 5. Midland-Ross conducts its business, as described herein, in various States of the United States and is thereby engaged in activity in or affecting commerce within the meaning of Section Four of the Federal Trade Commission Act, as amended, 15 U.S.C. 44, and Section 1 of the Clayton Act, 15 U.S.C. 12.

PAR. 6. Claude M. Blair was, until his resignation from Gould's board of directors on or about July 24, 1979, a member of the boards of directors of both Gould and Midland-Ross. He has been a director of Midland-Ross since 1974, and was a director of Gould from 1969 until his resignation.

PAR. 7. During all or part of the period that Claude M. Blair concurrently served as a director of Gould and Midland-Ross, the business of Gould and Midland-Ross included the manufacture and sale of various electrical products, including electrical busways and electrical conduit fittings.

PAR. 8. By the nature of their business as hereinabove described and the locations of their operations, Gould and Midland-Ross have been competitors, during all or part of the time period that Claude M. Blair concurrently served as a director of Gould and Midland-Ross, so that the elimination of competition by agreement between them would constitute a violation of the antitrust laws.

PAR. 9. The simultaneous membership of Claude M. Blair on the boards of directors of Gould and Midland-Ross constitutes a violation of Section 8 of the Clayton Act and Section 5(a)(1) of the Federal Trade Commission Act.

COUNT II

PAR. 10. Paragraphs One and Four are incorporated herein.

PAR. 11. Respondent Narco Scientific, Inc. ("Narco") is a corporation organized under the laws of the State of Delaware, with its principal place of business located at Fort Washington Industrial Park, Fort Washington, Pennsylvania. Narco has capital, surplus and undivided profits aggregating more than one million dollars.

PAR. 12. Respondent William C. Musham is an individual, with his

principal place of business located at Gould Inc., 10 Gould Center, Rolling Meadows, Illinois.

PAR. 13. Narco conducts its business, as described herein, in various States of the United States and is thereby engaged in activity in or affecting commerce within the meaning of Section Four of the Federal Trade Commission Act, as amended, 15 U.S.C. 44, and Section 1 of the Clayton Act, 15 U.S.C. 12.

PAR. 14. William C. Musham was, until his resignation from Narco's board of directors during January 1980, a member of the boards of directors of both Gould and Narco. He has been a director of Gould since 1976, and was a director of Narco from 1977 until his resignation.

PAR. 15. During all or part of the period that William C. Musham concurrently served as a director of Gould and Narco, the business of Gould and Narco included the manufacture and sale of electronic medical devices.

PAR. 16. By the nature of their business as hereinabove described and the locations of their operations, Gould and Narco have been competitors, during all or part of the time period that William C. Musham concurrently served as a director of Gould and Narco, so that the elimination of competition by agreement between them would constitute a violation of the antitrust laws.

PAR. 17. The simultaneous membership of William C. Musham on the boards of directors of Gould and Narco constitutes a violation of Section 8 of the Clayton Act and Section 5(a)(1) of the Federal Trade Commission Act.

DECISION AND ORDER

The Federal Trade Commission, having initiated an investigation of interlocking personnel relationships between Gould Inc. and other corporations, and William C. Musham, having been furnished thereafter with a copy of a draft of complaint which the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge William C. Musham with violation of Section 8 of the Clayton Act (15 U.S.C. 19) and Section 5 of the Federal Trade Commission Act (15 U.S.C. 45); and

William C. Musham, his attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by William C. Musham of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and

does not constitute an admission by William C. Musham that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that William C. Musham has violated the said Acts, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. William C. Musham is an individual with his office and principal place of business located at Gould Inc., 10 Gould Center, Rolling Meadows, Illinois.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of William C. Musham, and the proceeding is in the public interest.

ORDER

I

It is ordered, That the following definition shall apply herein:

"Product or service market" means any line of commerce in which a corporation's annual revenues exceed the lesser of:

(a) Five million dollars; or

(b) One-half of one percent of the total annual revenues of that corporation.

II

It is further ordered, That William C. Musham shall not be a director in any two or more corporations, any one of which has capital, surplus, and undivided profits aggregating more than one million dollars, engaged in whole or in part in commerce, if such corporations are, by virtue of their business and location of operation, competitors, so that the elimination of competition by agreement between them would constitute a violation of any of the provisions of any of the antitrust laws, providing that the revenues of either corporation derived from the product or service market(s) in which they are competitors exceed the lesser of:

(a) Ten million dollars; or
(b) One percent of the total revenues of that corporation.

If, after his election, competition arises in any product or service market between corporations upon which William C. Musham serves as a director such as would cause him to violate the terms of this paragraph, then William C. Musham shall not be liable under this paragraph until the date of the first annual meeting of shareholders following the time such competition arose.

III

It is further ordered, That William C. Musham shall:

(a) within sixty (60) days after the date of service of this order, file with the Commission a written report setting forth in detail the manner and form in which he has complied with this order; and
(b) file with the Commission such other reports of compliance as may be requested by the Commission.

IV

It is further ordered, That the obligations imposed upon William C. Musham under the terms of this order shall continue for a period of five years following the date of service of this order.

IN THE MATTER OF

SCHERING-PLOUGH CORPORATION

MODIFYING ORDER IN REGARD TO ALLEGED VIOLATION OF SEC. 2 OF THE CLAYTON ACT AND THE FEDERAL TRADE COMMISSION ACT

Docket C-2986. Decision, Aug. 10, 1979—Modifying Order, Aug. 22, 1980

This order reopens the proceeding and modifies the order issued on August 10, 1979, 44 FR 554712, 94 F.T.C. 307, by adding to Paragraph I of that order language that would permit the company, its subsidiaries, affiliates, divisions, successors and assigns to continue to market Solvex athlete's foot products, under license from the acquirer of the assets to be divested, until no later than December 31, 1980.

ORDER MODIFYING DECISION AND ORDER ISSUED AUGUST 10, 1979

The Federal Trade Commission having received respondent's request contained in its divestiture application dated June 23, 1980, to reopen this matter and to modify the consent order issued by the Commission on August 10, 1979, to allow respondent's subsidiary, Scholl, Inc., to continue to market Solvex athlete's foot products, under license from the acquirer of the divested assets, until December 31, 1980, and having placed such request on the public record for a period of thirty (30) days, and no comments thereon having been received, and having considered such request and determined that reopening and modification of the order is warranted:

It is ordered, That the proceeding be, and it hereby is, reopened.

It is further ordered, That Paragraph I of the order be, and it hereby is, modified to read as follows:

I

It is ordered, That, subject to the prior approval of the Federal Trade Commission, respondent Schering-Plough, through its officers, directors, agents, representatives, employees, subsidiaries, affiliates, divisions, successors and assigns, shall, within one (1) year from either the date Schering-Plough acquires Scholl or service of this Order, whichever comes later, divest the assets, tangible and intangible, acquired, improved or added by respondent as a result of its acquisition of Scholl and utilized by Scholl primarily for the manufacture, distribution or sale in the United States of Solvex athlete's foot products. Such assets shall include all raw material

reserves, inventory, machinery, equipment, trade names, trademarks, patents, licenses, research and development projects, good will and other property of whatever description; *provided, however,* that nothing in this provision shall prohibit or prevent Schering-Plough, its subsidiaries, affiliates, divisions, successors or assigns, from continuing to market Solvex athlete's foot products, under license from the acquirer of the assets to be divested, until no later than December 31, 1980.

Commissioner Bailey did not participate.

IN THE MATTER OF

TRANS WORLD ACCOUNTS, INC., ET AL.

MODIFYING ORDER IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket 9059. Order, Oct. 25, 1977—Modifying Order, September 2, 1980

In accordance with the mandate of the Court of Appeals for the Ninth Circuit, this order further modifies the Modified Order To Cease and Desist issued on July 25, 1979, 44 FR 49650, 94 F.T.C. 141, by inserting a new "Paragraph 3" which substitutes the term "lawsuit" for the phrase "legal action" as used in "Paragraph 3" of FTC's October 25, 1979 Order of Remand, 44 FR 66576, 94 F.T.C. 1051.

MODIFICATION OF MODIFIED ORDER TO CEASE AND DESIST

On July 25, 1979, the Commission entered a "Modified Order To Cease and Desist" in this matter, thereby effectuating those portions of its order of October 25, 1977 that had been affirmed and enforced by the Ninth Circuit Court of Appeals in *Trans World Accounts* v. *FTC,* 594 F.2d 212 (9th Cir. 1979). On October 25, 1979, the Commission entered an "Order on Remand", adding a new "Paragraph 3" to its order of July 25, 1979. Respondents appealed this order to the Ninth Circuit Court of Appeals, and, thereafter, respondents and the Commission entered into a stipulation before the court, which rendered its judgment modifying and enforcing as modified the order under appeal. Because both sides have waived any rights to seek further review of the court's order, it is now appropriate that the order of the Commission be rendered in accordance with the mandate of the court, 15 U.S.C. 45(i).

Therefore, it is ordered, That the Commission's "Modified Order To Cease and Desist" dated July 25, 1979, be further modified by the insertion of Paragraph 3 to read:

3. Misrepresenting directly or by implication, that a lawsuit with respect to an alleged delinquent debt has been or will be initiated, or misrepresenting in any manner the imminency of a lawsuit.

IN THE MATTER OF

PAY LESS DRUG STORES NORTHWEST, INC.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT AND SEC. 7 OF THE CLAYTON ACT

Docket C-3039. Complaint, Sept. 2, 1980—Decision, Sept. 2, 1980

This consent order requires, among other things, Pay Less Drug Stores Northwest, Inc. ("Northwest"), a Beaverton, Oregon, drug chain to refrain from acquiring Pay Less Drug Stores ("Pay Less"), located in the California communities of Lodi, Salinas and Livermore, because the acquisition eliminates the actual competition between Northwest and Pay Less "super drug stores." Further, the order requires that divestiture only be made to a person approved in advance by the Commission and the divested businesses continue as going concerns.

Appearances

For the Commission: *Laurence O. Masson.*

For the respondent: *Robert M. Heller, Kramer, Lowenstein, Nessen, Kamin & Soll,* New York City.

COMPLAINT

The Federal Trade Commission, having reason to believe that Pay Less Drug Stores Northwest, Inc. ("Northwest"), a corporation subject to the jurisdiction of the Commission, has acquired the stock and will acquire additional stock of Pay Less Drug Stores ("Pay Less"), a corporation, or has entered into an agreement and plan of reorganization and merger with Pay Less in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45, and that a proceeding in respect thereof would be in the public interest, hereby issues its complaint, pursuant to Section 11 of the Clayton Act, 15 U.S.C. 21, and Section 5(b) of the Federal Trade Commission Act, 15 U.S.C. 45(b), stating its charges as follows:

I. DEFINITIONS

1. For the purposes of this complaint the following definitions shall apply:

(a) "Super drug store" means a retail establishment, as distinguished from a traditional neighborhood or corner drug store, which

carries a much broader selection of traditional drug store merchandise as well as numerous lines not normally found in neighborhood drug stores and which caters to a relatively large trading area.

(b) "Lodi Area" means the city of Lodi, California.

(c) "Salinas Area" means the city of Salinas, California.

(d) "Livermore Area" means the city of Livermore, California, and its surrounding environs, including the unincorporated areas known as Dublin, California and San Ramon, California.

(e) "Prescription drugs" mean ethical drugs available at retail only by prescription.

II. PAY LESS DRUG STORES NORTHWEST, INC.

2. Northwest is a corporation organized, existing, and doing business under and by virtue of the laws of the State of Maryland with its headquarters office and principal place of business located, through February 15, 1980, at 10605 S.W. Allen Boulevard, Beaverton, Oregon and, after February 15, 1980, at 9275 S.W. Peyton Lane, Wilsonville, Oregon.

3. Northwest and its subsidiaries engage in the business of operating thirty-six super drug stores in communities in Oregon, twenty-eight super drug stores in communities in Washington, nineteen super drug stores in communities in California, and seven super drug stores in communities in Idaho. Northwest owns two of the super drug stores operated in Oregon and two in Washington; Northwest's other super drug store premises are leased. Northwest owns substantially all of the furniture and fixtures it uses in its stores with the exception of certain fixtures which are leased in Northwest's California super drug stores.

4. Northwest operates its super drug stores in California under the name "Value Giant."

5. For its fiscal year ending January 31, 1979, Northwest and its subsidiaries had total assets of $136,465,000 and net sales and other income of $347,959,000, yielding net earnings after income taxes of $9,853,000.

III. PAY LESS DRUG STORES

6. Pay Less is a corporation organized, existing, and doing business under and by virtue of the laws of the State of California with its principal offices at 8000 Edgewater Drive, Oakland, California.

7. Pay Less and its subsidiaries engage in the business of operating forty-eight super drug stores in communities in California,

two super drug stores in communities in Nevada and ten super drug stores in communities in Hawaii. All of Pay Less' super drug stores are leased, except for the premises owned and occupied by Pay Less' Sacramento, California store at 1012 "K" Street. Pay Less owns the fixtures and equipment used in most of its super drug stores.

8. Pay Less operates its super drug stores in California under the name "Pay Less."

9. For its fiscal year ending February 3, 1979, Pay Less and its subsidiaries had total assets of $102,477,000 and sales and other income of $278,354,000, yielding net earnings after income taxes of $2,854,000.

IV. JURISDICTION

10. At all times relevant herein, Northwest and Pay Less have been engaged in the ownership or operation of super drug stores in commerce as "commerce" is defined in Section 1 of the Clayton Act, as amended, 15 U.S.C. 12, and the businesses of Northwest and Pay Less are in or affect commerce, as "commerce" is defined in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. 44.

V. TENDER OFFER AND MERGER AGREEMENT

11. On January 17, 1980 Northwest commenced a tender offer to purchase, through its wholly owned subsidiary PNW Inc., any and all of the outstanding shares of common stock, no par value, of Pay Less at $22.50 net per share, the offer expiring on February 14, 1980 at 5:00 p.m. New York City time, unless extended, and being conditioned upon the valid tender of at least 917,000 shares prior to the expiration of the offer or any extension thereof. The purpose of the offer was to enable Northwest to acquire the entire equity interest of Pay Less. On February 4, 1980 Northwest amended its tender offer to increase, to $24.00 net in cash per share, the price it will pay for shares of Pay Less. In addition, Northwest extended the expiration of its tender offer to 12:00 midnight on February 15, 1980, unless further extended.

12. As of December 28, 1979 Northwest had obtained 269,000 shares, approximately 12.2% of the outstanding shares, of Pay Less in open market purchases. On or about February 27, 1980 Northwest acquired a controlling interest in Pay Less.

13. On February 1, 1980 Pay Less and Northwest, including certain wholly owned subsidiaries, entered into an agreement and plan of reorganization and merger, subject to the approval of a majority of shareholders of Pay Less, providing that Pay Less enter

into an agreement of merger whereby it become a wholly-owned indirect subsidiary of Northwest. A Pay Less shareholder's meeting has been called for March 31, 1980 for purposes of voting on the agreement and plan of reorganization and merger.

VI. TRADE AND COMMERCE

14. The relevant lines of commerce are the retail sale of prescription drugs or retail sales by super drug stores.

15. At all times relevant herein, Northwest and Pay Less are actual competitors in the Lodi Area, Salinas Area and in the Livermore Area.

VII. EFFECTS

16. The effects of the acquisition of Pay Less by Northwest may be substantially to lessen competition or tend to create a monopoly in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45, in the following ways, among others:

(a) actual competition between Northwest and Pay Less in the super drug store business in the Lodi Area will be eliminated;

(b) actual competition between Northwest and Pay Less in the retail sale of prescription drugs in the Lodi Area will be eliminated;

(c) actual competition between Northwest and Pay Less in the super drug store business in the Salinas Area will be eliminated;

(d) actual competition between Northwest and Pay Less in the super drug store business in the Livermore Area will be eliminated;

(e) actual potential competition between Northwest and Pay Less in the super drug store business in the Livermore Area will be eliminated;

(f) concentration in the super drug store business in the Lodi Area, Salinas Area or the Livermore Area will be increased or the possibility for eventual deconcentration may be diminished;

(g) concentration in the retail sale of prescription drugs in the Lodi Area will be increased or the possibility for eventual deconcentration may be diminished; and

(h) mergers or acquisitions between other super drug stores may be fostered or encouraged, causing a further substantial lessening of competition in the super drug store business.

Decision and Order

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the San Francisco Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45; and

The respondent, its attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it has reason to believe that the respondent has violated the said Acts, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent Pay Less Drug Stores Northwest, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Maryland, with its office and principal place of business located at 9275 S.W. Peyton Lane, in the City of Wilsonville, State of Oregon.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

Order

For the purposes of this Order the following definitions shall apply:

1. "Northwest" means Pay Less Drug Stores Northwest, Inc., a corporation organized, existing, and doing business under and by virtue of the laws of the State of Maryland with its principal offices,

through February 15, 1980, at 10605 S.W. Allen Boulevard, Beaverton, Oregon, and, after February 15, 1980, 9275 S.W. Peyton Lane, Wilsonville, Oregon, and each of its successors, assigns, subsidiaries, affiliates, directors, officers, employees and agents.

2. "Pay Less" means Pay Less Drug Stores, a corporation organized, existing, and doing business under and by virtue of the laws of the State of California with its principal offices at 8000 Edgewater Drive, Oakland, California, and each of its successors, subsidiaries and affiliates.

3. "Person" means any individual, corporation (including subsidiaries thereof), partnership, joint venture, trust, unincorporated association, or other business or legal entity.

4. "Super drug store" means a retail establishment which carries a much broader selection of drug store merchandise than a traditional neighborhood drug store, as well as numerous lines not normally found in a neighborhood drug store, and which caters to a relatively large trading area.

5. "Super drug stores subject to the terms and provisions of this Consent Order" mean

(1) the super drug stores operated at the following locations by Pay Less:

(a) 300 West Kettleman, Lodi, California; and
(b) 7201 Regional Street, Dublin, California; and

(2) the super drug store operated by Northwest at the following location:

(a) 1623 Chestnut Street, Livermore, California.

6. "Eligible person" means any person subject to prior approval by the Commission.

I.

It is ordered, and directed that within one (1) year of the date of service of the Consent Order, except in the case of the super drug store located at 1623 Chestnut St., Livermore, California, as to which the date for compliance shall be eighteen (18) months of the date of service of this Consent Order or within four months of respondent's opening a new super drug store in Livermore, whichever comes first, Northwest shall divest itself of all assets, title, interests, rights, and privileges, of whatever nature, tangible and intangible, presently owned or acquired in the future by Northwest, including without

limitation all buildings, equipment, fixtures, inventory, leasehold interests and other property of whatever description of each of the super drug stores subject to the terms and provisions of this Consent Order. Divestiture may be accomplished by the disposition of aforementioned super drug stores either separately or jointly.

II.

It is further ordered, That divestiture shall be made only to an eligible person and shall be in a manner which preserves the assets and business of the super drug stores subject to the terms and provisions of this Consent Order as going concerns and fully effective competitors.

III.

It is further ordered, That pending divestiture required by this Consent Order, Northwest shall not cause or permit any deterioration of the assets and businesses of the super drug stores subject to the terms and provisions of this Consent Order in a manner that impairs the viability of any such assets and businesses.

IV.

It is further ordered, That the divestiture ordered and directed by this Consent Order shall be made in good faith and shall be absolute and unqualified; *provided, however,* that an eligible person may give and Northwest may accept and enforce any bona fide lien, mortgage, deed of trust or other form of security on all or any portion of any one or more of the super drug stores subject to the terms and provisions of this Consent Order. If a security interest is accepted, in no event should such security interest be interpreted to mean that Northwest has a right to participate in the operation or management of such stores. In the event that Northwest as a result of the enforcement of any bona fide lien, mortgage, deed of trust or other form of security interest reacquires possession of any one or all of the aforementioned super drug stores, then Northwest shall divest the reacquired assets and business in accordance with the terms of this Consent Order within six (6) months of the reacquisition.

V.

It is further ordered, That Northwest shall use its best efforts to fulfill and complete the current expansion plans of Pay Less with

respect to the lease, construction, opening and operation of new super drug stores to be located in San Ramon, California and Livermore, California.

VI.

It is further ordered, That, in the event Northwest has not terminated the lease of the premises of its super drug store located at 1045 N. Main St., Salinas, California, and vacated the premises on or before March 31, 1980, Northwest shall divest itself of the aforesaid super drug store within one (1) year of the date of service of this Consent Order and otherwise in the same manner as the divestiture of super drug stores subject to the terms and provisions of this Consent Order.

VII.

It is further ordered, That Northwest shall within ninety (90) days from the date of service of this Consent Order and every ninety (90) days thereafter until divestiture is completed and the new San Ramon and Livermore super drug stores opened submit in writing to the Commission a report setting forth in detail the manner and form in which respondent intends to comply, is complying, and has complied with the terms of this Order and such additional information relating thereto as may from time to time be required.

VIII.

It is further ordered, That Northwest notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondent, such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporation which may affect compliance with the obligations arising out of this Consent Order.

IN THE MATTER OF

STERLING DRUG INC., ET AL.

Docket 8919. Interlocutory Order, Sept. 3, 1980

ORDER DENYING STERLING'S APPLICATION FOR INTERROGATORIES

Respondent Sterling Drug Inc., ("Sterling") seeks authorization to serve complaint counsel with interrogatories concerning the issuance of a Federal Trade Commission press release dated April 17, 1980. Sterling's application was certified to us by the Administrative Law Judge on May 15, 1980; the law judge has declined to rule on the matter because he believes that Rules 3.31(b)(1) and 3.35 do not authorize him to do so.

The press release involved here announced the Commission's initial acceptance of a consent agreement with Dancer-Fitzgerald-Sample, Inc. ("DFS"), an advertising agency that was named as a respondent in this proceeding due to its former responsibility for handling Sterling's Bayer Aspirin and Cope accounts. The agreement specifically limited the superiority and other types of claims that DFS could make in the future on behalf of Bayer Aspirin, Bayer Children's Aspirin, Cope, and any other over-the-counter analgesic. Sterling claims that the press release on this agreement was deceptive, however, and led to erroneous news reports that Bayer (i.e., Sterling) had agreed not to claim that its aspirin was superior to others. More specifically, Sterling contends that the release should at least have stated that DFS no longer handles advertising for Sterling and that Sterling is "now vigorously defending" against Commission charges at trial. In fact, the company's basic position appears to be that the press release should not have named any of its products at all since DFS is no longer connected with them in any way.

Complaint counsel have stated that they reviewed the press announcement prior to dissemination. Sterling contends that this fact raises the issue of prosecutorial misconduct and that interrogatories are necessary to establish complaint counsel's role in approving the release.

We do not consider lightly the kinds of concerns which Sterling has raised, for we recognize the impact that an agency press release may have on a company's reputation and competitive position. It is essential, therefore, that every effort be made to ensure that press releases are accurate and fair, and are not likely to be misconstrued by the news media. However, it is also clear that the Commission has an important obligation to inform the public of its activities, and

that the Commission's authority to publish announcements on the progress of agency proceedings is not eclipsed by the possibility that a respondent's goodwill might suffer. *Federal Trade Commission* v. *Cinderella Career & Finishing Schools, Inc.*, 404 F.2d 1308 (D.C. Cir. 1968). Thus, a respondent who objects to a press release would have no legally enforceable claim for relief unless it can at least show that it was injured by an inaccurate or discriminatory announcement. *See id.* at 1314. Assuming that such a showing would warrant some form of remedy—and we withhold judgment on that issue—the respondent should not be entitled to take the extraordinary step of serving interrogatories on complaint counsel without offering some reason to connect the inaccurate or discriminatory statement to prosecutorial abuse.[1] In this case, we find no inaccuracies in the release and no indications of prosecutorial abuse.[2]

The company argues that the announcement was inaccurate because it failed to make clear that DFS no longer had a direct stake in the case and that Sterling itself had strongly denied Commission charges. We disagree. The proposed disclosure regarding DFS might have suggested that the agency settled because it no longer had a sufficient interest to continue litigation. However, the accuracy of such an explanation is speculative and its relevance to the consent agreement strikes us as marginal. Sterling may believe that such a disclosure would tend to support its position opposing the charges in the complaint, but staff members should not be required to prepare press releases to achieve that purpose. In any event, the release stated that DFS, in accepting the consent agreement, did not admit that it had violated the law.

Similarly, the release noted that charges against Sterling and another advertising agency were still pending. Perhaps this statement was not so emphatic as Sterling would have wished, but we do not believe that there was an obligation to ensure that the release disclosed the vigor of Sterling's opposition to the charges made against it.

Finally, Sterling argues that the release should not have "emphasized" its products. However, the agreement signed by DFS covers claims for those products. One may thus expect that an accurate summary of this agreement would name Sterling's products. Fur-

[1] However, a respondent or any other party affected by a Commission press release may always seek the publication of corrected press releases by contacting the Office of Public Information (OPI), or by submitting a formal request to the Commission itself.

[2] It should be noted that OPI has primary responsibility for drafting press announcements, and that the function of other staff members, such as complaint counsel here, is merely to consult with OPI as needed. *See* FTC Operating Manual Section 17.2.2 (1980); *cf. id.* Section 5.14.6.13. In this and in other respects, complaint counsel are expected to follow Rule 7-107(H) of the Code of Professional Responsibility. *See The Raymond Lee Organization, Inc.*, 89 F.T.C. 208 (1977).

thermore, since the complaint in this proceeding was directed specifically against advertisements of Sterling analgesics, it is hardly inappropriate that a settlement with one of the respondents should clearly identify the products concerned.

We therefore deny the respondent's application. Accordingly,

It is ordered, That respondent's application to serve interrogatories on complaint counsel be, and hereby is, denied.

Commissioner Pitofsky did not participate.

IN THE MATTER OF

MACMILLAN, INC., ET AL.

FINAL ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket 9110. Complaint May 23, 1978—Decision, Sept. 4, 1980

This order requires a New York City publishing firm and its Chicago, Ill. subsidiary, LaSalle Extension University, among other things, to cease, in connection with the advertising and sale of correspondence courses, misrepresenting the school's admission policy; the need or demand for graduates of their courses; the employment prospects and potential earnings available to them; and the requirements or qualifications necessary to obtain employment in their chosen fields. Advertisements containing any job or earnings claim must include a disclaimer stating that "Graduation from this course does not guarantee you will get a job;" and testimonials which do not reflect the typical student experience must advise that the described experience is atypical. Further, if respondents represent to any prospective student that there is an employment demand for graduates of a relevant course, they must clearly and conspicuously disclose specified information regarding the vocation success rate of previous students. Additionally, respondents are prohibited from misrepresenting or failing to disclose material facts concerning a student's financial obligations upon enrollment, and right to cancellation and refund.

Appearances

For the Commission: *Alice S. Perlin.*

For the respondent: *Bella Linden* and *Frederick F. Greenman, Linden & Deutsch,* New York City and *Abe Fortas, Fortas & Koven,* Washington, D.C.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that Macmillan, Inc., a corporation, and LaSalle Extension University, a corporation, hereinafter sometimes referred to as respondents, have violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its Complaint stating its charges in that respect as follows:

PARAGRAPH 1. Respondent Macmillan, Inc. (hereinafter sometimes referred to as Macmillan) is a corporation, organized, existing, and doing business under and by virtue of the laws of the State of

Delaware, with its principal place of business located at 866 Third Ave., New York, New York.

Respondent LaSalle Extension University (hereinafter sometimes referred to as LEU) is a corporation organized, existing, and doing business under and by virtue of the laws of the State of Illinois, with its principal office and place of business located at 417 South Dearborn St., Chicago, Illinois. Respondent LaSalle Extension University is a wholly-owned subsidiary of respondent Macmillan, Inc.

The aforementioned respondents have cooperated, and acted together in carrying out the acts and practices hereinafter set forth. Respondent Macmillan has known of, condoned and approved, expressly or tacitly, the acts and practices of respondent LEU hereinafter set forth. Respondent Macmillan has assumed financial responsibility for respondent LEU.

PAR. 2. Respondents have been, and are now, engaged in the advertising, promotion, formulation, offering for sale, sale and distribution of correspondence courses of instruction to the public involving high school courses and those purporting to prepare completing students thereof for employment, advancement, or increased earnings in the fields of air conditioning and refrigeration, interior decorating, computer programming, hotel/motel executive training and various other fields of employment. Their volume of business has been, and is, substantial. [2]

PAR. 3. In the course and conduct of their aforesaid business, respondents have disseminated and caused to be disseminated by various means in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, certain advertisements concerning their correspondence courses, including but not limited to advertisements inserted and published in newspapers and magazines of general interstate circulation, by means of brochures, pamphlets and other promotional materials disseminated through the United States mail, commercial announcements on radio and television transmitted across state lines, and by other means for the purpose of obtaining leads or prospects for the sale of such correspondence courses and for the purpose of inducing the purchase of such correspondence courses.

Respondents have caused, and now cause, said courses of instruction to be shipped and distributed from their places of business or sources of supply to purchasers and prospective purchasers thereof located in various States of the United States other than the state of origination. Respondents transmit and receive and have caused to be transmitted and received, in the course of advertising, offering for sale, sale and distribution of such correspondence courses, advertis-

ing and promotional materials, invoices, checks, enrollment contracts, retail installment contracts, collection notices and various other commercial papers or documents to and from prospective students and students located in various States of the United States, other than the state of origination.

Respondents maintain, and at all times mentioned herein have maintained, a substantial course of trade in such correspondence courses, and other products or services in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended.

PAR. 4. In the course and conduct of their aforesaid business, for the purpose of obtaining leads or prospects for the sale of their correspondence courses and for the purpose of inducing the purchase of such correspondence courses, respondents have made numerous statements and representations in oral sales presentations to prospective students and in magazines, brochures, and other media regarding opportunities for employment or advancement, occupational demand, earnings potentials, the qualifications of students who complete respondents' correspondence courses, the instruction and assistance available to students, and other related matters.

PAR. 5. By and through the use of the aforesaid statements and representations and others of similar import and meaning, but not expressly set forth herein, respondents have represented, directly or by implication that:

1. There is substantial need or demand for students who complete respondents' correspondence courses in the positions and career fields for which respondents train such students. [3]

2. Students completing respondents' correspondence courses will receive high wages or salaries from employment in the positions or career fields for which respondents train such students.

3. Students completing respondents' correspondence courses are qualified thereby to secure employment in the positions or career fields in which respondents train such students without further training or experience.

4. Respondents have admissions requirements and procedures to screen prospective students and to determine whether such prospective students have the qualifications and ability to assimilate successfully and complete respondents' correspondence courses.

PAR. 6. In truth and in fact:

1. There is not substantial need or demand for students complet-

ing respondents' correspondence courses in the positions or career fields for which respondents train such students.

2. In many instances students completing respondents' correspondence courses have not received high wages or salaries from employment in positions for which respondents train such students.

3. In many instances students completing respondents' correspondence courses are not thereby qualified to secure employment in the positions or career fields in which respondents train such students without further training or experience.

4. Respondents do not screen prospective students. To the contrary, respondents require few qualifications of prospective students and accept all or most persons for enrollment in such courses who are willing to execute a contract to pay for such correspondence courses. Any admission requirements or procedures used by respondents do not determine whether such prospective students have the qualifications and ability to assimilate successfully and complete respondents' correspondence courses; to the contrary, any such admission requirements or procedures are used by respondents as promotional devices to induce the purchase of respondents' correspondence courses.

Therefore, the statements and representations set forth in Paragraphs Four and Five were and are false, misleading, deceptive or unfair acts or practices.

PAR. 7. Through the use of the aforesaid advertisements, materials, oral presentations and otherwise, respondents have represented, directly or by implication, that there is or will be a substantial need or demand for all or most of the students enrolled in respondents' correspondence courses in [4]career fields for which respondents train them. Respondents at the time of said representations had no reasonable basis adequate to support such representations. Therefore, the aforesaid acts and practices were and are unfair acts or practices.

PAR. 8. In the further course and conduct of their aforesaid business, respondents have represented that students who have finished respondents' high school courses and received a diploma therefrom, have, on that basis alone, qualified themselves as high school graduates and were recognized as such by the state in which they were domiciled or worked.

PAR. 9. In truth and in fact all or virtually all of the States of the United States require a person not a graduate of a resident high school to take a general equivalency or other similar test in order to be recognized as a high school graduate.

Therefore, the aforesaid acts and practices were and are false, misleading, deceptive or unfair acts or practices.

PAR. 10. Respondents further have offered for sale correspondence courses intended to give students high school training without disclosing that all or virtually all States of the United States allow a person over 19 years of age to take a high school equivalency or similar test which would qualify the person as the equivalent of a high school graduate who had received a diploma, without the necessity of taking any courses. Therefore, the aforesaid acts and practices were and are false, misleading, deceptive or unfair acts or practices.

PAR. 11. Through the use of the aforesaid advertisements, materials, oral presentations and otherwise, and for their purpose of inducing the purchase of correspondence courses, respondents have degraded, debased or disparaged the present or potential career opportunities, education, training, family standing, community status, self-image or other personal characteristics of prospective students. Further, respondents represent, directly or by implication, that such prospective students can alter or improve such personal characteristics through respondents' correspondence courses.

The effect of the aforesaid disparagements and representations has been to aggravate and continue the unfair and deceptive effect of the acts and practices set forth herein. Therefore, the aforesaid acts and practices of respondents were and are unfair acts or practices.

PAR. 12. In the further course and conduct of their aforesaid business, respondents have failed to disclose or have misrepresented the true nature of the financial obligation to students who signed enrollment agreements or contracts.

The deceptions resulting from the acts or practices described in this Paragraph Twelve are continuing, in many instances, through the period of the students' enrollment and concomitant deferred payment obligations. [5]

Therefore, the aforesaid acts and practices of respondents were and are false, misleading, deceptive or unfair acts or practices.

PAR. 13. In the further course and conduct of their aforesaid business, and in furtherance of their purpose of inducing prospective students to execute enrollment contracts for the purchase of their correspondence courses, respondents and their employees, sales force members, and representatives, through the use of the false, misleading and deceptive statements, representations and practices set forth herein in this Complaint, have been able to induce prospective students into executing enrollment contracts upon initial contact without affording such students sufficient time to carefully consider

the purchase of correspondence courses. Therefore, the aforesaid are unfair acts or practices.

PAR. 14. Through the false, misleading and deceptive acts or practices, and the unfair acts or practices herein set forth in this Complaint, respondents have induced students and other persons or entities to pay, or contract to pay, to respondents substantial sums of money to purchase or pay for respondents' correspondence courses. In many instances such monies were paid to and received by respondents although such courses were of little value to students in fulfilling the expectations created by respondents' representations or contracts. Respondents have received the aforesaid monies and have failed to offer to refund such sums to, or to rescind contractual obligations of, many students and other persons or entities participating in the financing of such correspondence courses.

By inducing students and other persons or entities to pay, or contract to pay, to respondents substantial sums of money for respondents' correspondence courses where such correspondence courses are of little value to students and by failing to offer or refund such sums to, or to rescind the contractual obligations of many students and other persons or entities where such courses are of little value, respondents have engaged in unfair acts and practices.

Therefore, the said acts or practices constitute unfair acts or practices in violation of Section 5 of the Federal Trade Commission Act.

PAR. 15. By and through the use of the aforesaid acts and practices, statements and representations, respondents have placed in the hands of others the means and instrumentalities by and through which they mislead and deceive the public in the manner hereinabove alleged.

PAR. 16. The use by respondents of the aforesaid false, misleading, unfair or deceptive statements, representations, acts and practices, has had, and now has, the capacity and tendency to mislead and deceive a substantial portion of members of the general public into the erroneous and mistaken belief that said statements and representations were, and are, true and complete, [6]and to induce a substantial number thereof to purchase respondents' correspondence courses by reason of said erroneous and mistaken beliefs.

PAR. 17. The aforesaid acts and practices of respondents, as herein alleged, were and are all to the prejudice and injury of the public and constituted, and now constitute, unfair or deceptive acts or practices in or affecting commerce, in violation of Section 5 of the Federal Trade Commission Act, as amended.

Initial Decision by Theodor P. von Brand, Administrative Law Judge

April 28, 1980

Preliminary Statement

The complaint charges that Macmillan, Inc. and LaSalle Extension University in the course of operating a correspondence school violated Section 5 of the Federal Trade Commission Act.

The complaint alleges essentially that respondents misrepresented: [2]

1. the occupational demand for respondents' graduates in the fields for which respondents train their students.
2. the earnings potential of students completing respondents' correspondence courses.
3. that graduates of respondents' courses would be qualified to secure employment in the fields, in which respondents trained such students, without further training or experience.
4. that respondents had admission requirements to screen prospective students to determine that such students had the qualifications and ability to successfully assimilate and complete respondents' courses.

(Paragraphs Four and Five)

The complaint substantially alleges:

That respondents had no reasonable basis to support the representation that a substantial need or demand existed for all or most of the students enrolled in respondents' correspondence courses in the fields for which they trained.

(Paragraph Seven)

That respondents, as part of their sales or promotional effort, debased or disparaged the career potential, self image or other personal characteristics of prospective students, and that respondents further represented directly or by implication that prospective students could alter or improve such personal characteristics through respondents' correspondence courses. It is charged that such disparagement was unfair since it aggravated and continued the unfair and deceptive effect of the other acts and representation alleged illegal in the complaint.

(Paragraph Eleven)

[3]That respondents failed to disclose or misrepresented the true nature of the financial obligation incurred by those signing enrollment agreements or contracts.

(Paragraph Twelve)

That respondents through the use of false misleading and deceptive statements and practices alleged in the complaint induced prospective students to execute enrollment contracts without affording them sufficient time to consider such purchase.

(Paragraph Thirteen)

That respondents through the deceptive or unfair acts and practices alleged by the complaint induced students or others to pay substantial sums of money for their correspondence course. In many instances, it is alleged, such monies were paid to and received by respondents "although such courses were of little value to the students in fulfilling the expectations created by respondent's representations or contracts." The failure to refund or offer to refund such sums where the courses were of little value to students is alleged to be unfair.

(Paragraph Fourteen)

Paragraphs Eight, Nine, and Ten of the complaint alleged various misrepresentations concerning respondents' high school courses. No evidence was offered in support of these charges and they were dismissed.

This matter is now before the undersigned for decision based on the allegations of the complaint, the answers, the evidence of record and the proposed findings of fact, conclusions and briefs filed by the parties. All proposed findings of fact, conclusions and agreements not specifically found or accepted herein are rejected. The undersigned, having considered the entire record and the contentions of the parties, makes the following findings of fact and conclusions, and issues the orders set out herein. [4]

Findings of Fact

I. Identity of Respondents and the Nature of Their Business

1. Respondent Macmillan, Inc. (hereinafter cited as Macmillan) is a corporation organized, existing and doing business under and by

virtue of the laws of the State of Delaware with its principal office and place of business located at 866 Third Ave., New York, New York (Comp. Par. 1; Macmillan Ans. Par. 1).

2. Macmillan is engaged, directly and through its subsidiaries, in five lines of business: publishing, educational instruction, printing, manufacture of musical instruments, and film and book club distribution (CX 376C–D, 377D, 378E, 379B).

3. Respondent LaSalle Extension University (hereinafter cited as LaSalle) is a wholly-owned subsidiary of Macmillan (Comp. Par. 1; LaSalle Ans. Par. 1; Macmillan Ans. Par. 1). LaSalle is a corporation organized, existing and doing business under and by virtue of the laws of the State of Illinois with its principal office and place of business located at 417 South Dearborn St., Chicago, Illinois (Comp. Par. 1; LaSalle Ans. Par. 1). It operates the Wayne School as an unincorporated division of LaSalle Extension University (RA 15).

4. LaSalle has been and is now engaged in the offering for sale and the sale of correspondence school education courses to the public (Comp. Par. 2, LaSalle Ans. Par. 2).

5. LaSalle is accredited by the National Home Study Council (CX 330). It operates under annual Certificates of Approval issued by the Office of the Superintendent of Education, State of Illinois and is licensed to do business in 17 other states (CX 327J).

6. LaSalle, as of 1975, offered correspondence courses in the following areas:

Accounting
Administrative Assistant
Associate Degree Program in Accounting
Associate Degree Program in Banking and Finance
Associate Degree Program in Business Management [5]
Associate Degree Program in Hotel and Restaurant Administration
Bachelor of Science in Commerce and Social Studies
Banking and Finance
Basic Computer Programming
Business Management
California Law Program
Drafting
Electronics, FCC License
Law for Executive Leadership
Hotel/Motel Executive Training
Interior Decorating
LaSalle Writing Program

Personnel Management
Real Estate
Restaurant/Club & Food Management
Secretarial Training
Stenotype
Supervisory Management
Traffic and Transportation
Writing
Basic Air Conditioning and Refrigeration Service
Basic Diesel Mechanics
Dental Office Assistant
High School

(CX 151R). New enrollments in the Basic Computer Programming course were terminated at approximately the end of 1977.

7. In the period 1973–1977, LaSalle enrolled the following numbers of students in its courses:

	Total (All Courses)	*Computer Programming*	*Air Conditioning & Refrigeration Service*	*Interior Decorating*
1973	86,913	2,363	3,575	10,282
1974	92,551	2,732	2,870	11,086
1975	53,187	1,500	1,477	6,744
1976	37,283	1,117	872	5,108
1977	34,704	1,038	857	3,901

(RA 22, 23, 24, 25).

8. In the course and conduct of its business, LaSalle disseminated and caused to be disseminated by various means in [6]or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, certain advertisements concerning its correspondence courses, including but not limited to advertisements inserted and published in newspapers and magazines of general interstate circulation. It has also utilized brochures, pamphlets and other promotional materials disseminated through the United States mail, commercial announcements on radio and television transmitted across state lines, as a means to obtain leads or prospects for the sale of correspondence courses and to induce the purchase of such courses (Comp. Par. 3; LaSalle Ans. Par. 3).

9. LaSalle is engaged in commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended, in connection with

the offering for sale and sale of correspondence school courses for compensation (Comp. Par. 3; LaSalle Ans. Par. 3).

10. LaSalle maintains and has maintained a substantial course of trade in its correspondence courses and other products or services in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended (Comp. Par. 3; LaSalle Ans. Par. 3).

11. Macmillan's sales and revenues in the period 1973–1977 were as follows:

1973	$420,372,000
1974	466,584,000
1975	477,347,000
1976	493,425,000
1977	512,727,000

(RA 21). Its volume of business has been, and is, substantial.

12. LaSalle's sales and revenues for the years 1973–1977 were as follows:

1973	$35,573,000
1974	36,582,000
1975	21,737,000
1976	17,192,000
1977	14,505,000

(RA 20). Expressed as a percentage of Macmillan's sales and revenues, LaSalle's contribution was:

1973	8.46%
1974	7.74 [7]
1975	4.55
1976	3.48
1977	2.83

(RA 20).

13. LaSalle's volume of business has been, and is, substantial.

II. Interrelationship of Macmillan and LaSalle

A. Corporate Officials

14. On August 30, 1978, Macmillan's Corporate Officials were the following:

Chairman of the Board and Chief Executive Officer (RA 1)	Raymond C. Hagel
President and Chief[1] Operating Officer (from June 8, 1976) (RA 2)	Robert A. Barton
Vice-Chairman of the Board, Deputy Chief Operating Officer, Director (RA 9)	Alan L. Baker
Senior Vice President and Controller (RA 8)	James P. Kressler
Treasurer and Assistant Secretary (RA 6)	Gordon H. DeWerth
Secretary (RA 5)	Jeffrey R. Minot

15. LaSalle's principal officers as of September 1978 were:

[8]President and Chairman of the Board	Robert A. Barton[2]
Vice-President	Robert Cornwell
Vice-President	Charles Marshall
Vice-President	Calvin Israel
Controller	John Sadler

(CX 110B; RA 2).

1. Overlap between Macmillan and LaSalle Officials and Involvement of Macmillan Officials in LaSalle's Business

16. Robert A. Barton, Director, President and Chief Operating Officer of Macmillan was also Director, Chairman of the Board and President of LaSalle (RA 2). Mr. Barton reported directly to Macmillan's Chairman of the Board (Barton 1795). As President of Macmillan, he was responsible for the assets of Macmillan and its subsidiaries as well as Macmillan's business strategy as carried out by its subsidiaries (Barton 1794).

17. Alan L. Baker, a Director, Vice-Chairman of the Board and Deputy Chief Operating Officer of Macmillan and a Director of LaSalle shared certain of Mr. Barton's responsibilities in managing Macmillan's business. He reported directly to Mr. Barton (RA 9; Barton 1795–96).

18. James P. Kressler, Senior Vice President and Controller of Macmillan was a Director of LaSalle and LaSalle's Executive Vice-

[1] Mr. Barton was Executive Vice President of Macmillan in the period 1973–June 8, 1976 (RA 2).

[2] Mr. Barton held these positions from May 1975 and was still in these positions as of August 30, 1978 (RA 2).

President of Finance (RA 8). Mr. Kressler reported directly to Macmillan's Chairman of the Board (Barton 1797). As Macmillan's senior financial officer, he had primary responsibility for the books and accounts of Macmillan and its subsidiaries. He was responsible for the auditing, accounting policy and the financial reporting system of the parent company and its subsidiaries (Barton 1796).

19. Gordon H. DeWerth was Treasurer and Assistant Secretary of Macmillan and Treasurer and a Director of LaSalle (RA 6). Mr. DeWerth, who reported directly to Macmillan's Controller was responsible for Macmillan's consolidated cash management, [9]investment of excess cash for foreign exchange, and pension investments (Barton 1796–97; DeWerth 1834).

20. The predecessor of Macmillan's current Treasurer and Assistant Secretary had also concurrently held the position of Director and Treasurer in LaSalle (RA 4).

21. Jeffrey A. Minot was Secretary of both Macmillan and LaSalle on August 30, 1978 (RA 5).

22. The predecessor of Macmillan's current Secretary was concurrently Secretary of LaSalle (RA 7).

23. The Chairman of the Board of Macmillan selected LaSalle's directors in consultation with Mr. Barton (Barton 1798). It is common practice to have some employees of Macmillan as Directors of LaSalle (Barton 1798–99).

24. There was extensive overlap in the positions of the officials and directors of Macmillan and LaSalle. See the following chart showing the positions held by certain key officials in the parent company and LaSalle as of January 1, 1977:

Robert A. Barton
Director, President, Chief Operating Officer, Macmillan
Director, Chairman of the Board, President, LaSalle
Warren B. Smith
Senior Vice-President, Macmillan
Director, LaSalle
Alan L. Baker
Director, Vice Chairman of the Board, Deputy Chief Operating Officer, Macmillan
Director, LaSalle
James P. Kressler
Senior Vice-President, Controller, Macmillan
Director, Vice-President, Finance, LaSalle
Gordon H. DeWerth
Treasurer, Assistant Secretary, Macmillan

Director, Treasurer, LaSalle
Jeffrey R. Minot
Secretary, Macmillan
Secretary, LaSalle [10]

B. Duties and Reporting Relationships of LaSalle Officials

25. Robert A. Barton, LaSalle's Chairman of the Board and President, while serving as Macmillan's President, Chief Operating Officer and Director, was responsible for the business strategy of LaSalle, including development of long and short-range plans devised to achieve the long-range objectives. He had responsibility for decisions respecting the type of business to be pursued by LaSalle, the manner in which it would be pursued, and LaSalle's investment decisions (Barton 1797).

Mr. Barton represented LaSalle on the National Home Study Council (hereinafter cited as NHSC) (Barton 1829–30). He signed and certified as correct the LaSalle Self-Evaluation Report (CX 327), which had been prepared for purposes of LaSalle's accreditation by that organization. Mr. Barton submitted the report to the NHSC (CX 327B). He was also responsible for implementing the changes in LaSalle recommended by the NHSC (Barton 1830).

26. In 1978, Alan L. Baker, Macmillan's Deputy Chief Operating Officer and Vice Chairman of the Board, received monthly financial and operations reports from LaSalle (CX 554–63, 565–79; see Finding 17). He related the results to Mr. Barton (Barton 1802–03). Before 1978, Mr. Barton had received monthly reports directly from LaSalle (CX 501–51; Barton 1802–04).

27. John Sadler, the Controller of LaSalle and its chief financial officer also acted as LaSalle's Chief Operating Officer in 1978 (Barton 1810–11; DeWerth 1838–39). Mr. Sadler, who received reports from LaSalle's Vice Presidents and other personnel, consolidated such reports and reported in turn to Alan L. Baker, Vice Chairman of the Board and Deputy Chief Operating Officer of Macmillan (Barton 1798; 1804).

28. In 1979, LaSalle hired Henry Broido to head up a continuing education group and to take responsibility for overall operations at LaSalle. Certain changes in the reporting relationships occurred at that time. Mr. Barton thereafter received monthly operations and financial reports from Mr. Broido (Barton 1820–21).

29. John Sadler, LaSalle's Controller and its chief financial officer (Barton 1810–11; DeWerth 1838–39) commenced [11]reporting

to Mr. Broido after the latter was employed by LaSalle (Barton 1820).

30. Charles B. Marshall, LaSalle's Vice-President for Education (Marshall 1887) had submitted monthly reports to Alan Baker, Macmillan's Vice Chairman of the Board and Deputy Chief Operating Officer through Mr. Sadler, the LaSalle Controller (CX 575–79; Marshall 1892–93). These written reports concerned educational services, regulatory and financial matters, personnel matters and extraordinary events (Marshall 1897–98). Subsequent to Mr. Broido's appointment in 1979, Mr. Marshall reported to him (Marshall 1892–93).

31. Calvin Israel, LaSalle's Vice-President and Field Sales Manager since 1972 (Israel 1987) had overall responsibility for the field sales operation (Israel 1988). Mr. Israel reported to Alan Baker, Macmillan's Vice Chairman of the Board and Deputy Chief Operating Officer through John Sadler, the LaSalle Controller (CX 565–74; Israel 1988). Previously, he had reported to Sadler's predecessors in the position of LaSalle's chief operating officer (Israel 1988).

32. Robert Cornwell, LaSalle's Vice-President for Advertising since 1973 had overall responsibility for advertising and mail order sales (Barton 1797; Cornwell 1867). Mr. Cornwell reported to Alan Baker, Macmillan's Vice Chairman of the Board and Deputy Chief Operating Officer with copies of the reports to John Sadler, who was LaSalle's Controller, and who also acted as LaSalle's Chief Operating Officer (CX 554–63; Cornwell 1868–69). Mr. Cornwell had channeled previous reports to Sadler's predecessors as LaSalle's Chief Operating Officer (Cornwell 1867–68). Beginning in 1979, he reported to Mr. Broido (Cornwell 1867).

33. David Hetzel was LaSalle's Vice-President for Student Relations from 1971 through 1977 (Hetzel 3063–64). Hetzel was responsible for the student relations department, enrollment department, clerical operations department, systems, purchasing, warehouse, shipping and receiving. The Student Relations Department was responsible for maintenance of student grade records, responses to student inquiries and complaints, providing study materials, and calculating tuition (Hetzel 3064–65).

34. Douglas Linde has been Assistant to the President of LaSalle and University Administrative Officer for over 10 years (Linde 1852–53). His responsibilities included liaison and filing of documents with various federal and state agencies, submission of license applications to state agencies, and handling of third-party inquiries relating to students (Linde 1853). Mr. Linde reported in the past to Mr. Sadler and to Mr. Sadler's predecessors as chief operating officer of LaSalle

(Linde 1855–57). His reports were written monthly activity reports covering his areas of responsibility [12](Linde 1855–57). Subsequently, he reported to Mr. Broido who took charge of LaSalle's operations in 1979 (Linde 1854–55).

35. Gordon DeWerth, Treasurer of Macmillan and Treasurer of LaSalle, had no direct reporting relationship at LaSalle; his reporting relationship was at Macmillan. As Treasurer of LaSalle, he reported to Mr. Kressler, the parent company's Senior Vice President of Finance (Dewerth 1836–37). His responsibilities at LaSalle were limited to cash management, insuring that LaSalle had sufficient cash to meet its requirements and that excess cash, when available, was loaned to Macmillan (DeWerth 1836).

C. LaSalle Reports to Macmillan

36. Macmillan executives received, on a monthly basis, written activity reports from LaSalle's personnel respecting the ongoing operations of LaSalle (Barton 1803–05). Although the recipient of these reports has varied, since 1973 the chief operating officer at LaSalle has submitted the reports to either Mr. Barton directly or to Mr. Baker, who then prepared a monthly report on LaSalle's operations for Mr. Barton (Barton 1805). Using the information contained in these reports, Mr. Barton prepared reports, which contained information on LaSalle's operations, for Macmillan's Chairman of the Board. He also reported, orally, to the Macmillan Board of Directors (Barton 1805–06).

37. Macmillan kept apprised of LaSalle's financial condition through monthly financial statements submitted by Mr. Sadler to the accounting manager of Macmillan's corporate accounting department (DeWerth 1842). These financial statements were then incorporated into Macmillan's annual report to shareholders and into financial statements filed with the Securities and Exchange Commission (DeWerth 1842–43).

38. Additionally, Mr. DeWerth submitted a monthly report to Messrs. Hagel, Barton, Baker and Kressler covering long and short-term cash forecasting, special projects, and stock reports (DeWerth 1839–40). This report was prepared in both consolidated and subsidiary-by-subsidiary form (DeWerth 1840–41).

39. LaSalle's executives prepared, on a yearly basis, a long-range plan which set forth, in both narrative and financial terms, LaSalle's business strategy for the succeeding five years (CX 425; Barton 1809–10). The long-range plan was a collective effort of LaSalle's management and was approved by Macmillan following discussions between

LaSalle's chief operating officer and Robert Barton and Alan Baker (Barton 1810–11). [13]

40. In addition to the long-range plan, LaSalle prepared an annual plan which expressed, in both narrative and financial terms, what LaSalle planned to do in any given year. The annual plan, an implementation of the strategy developed in the long-range plan, was approved by Macmillan after consultation between Messrs. Barton, Baker and LaSalle's chief operating officer (Barton 1809–11, 1813).

41. LaSalle executives have dealt directly with Macmillan executives on questions relating to LaSalle's operations. In 1978, for example, Mr. Baker went to LaSalle on three or four occasions and met with LaSalle's operating committee, composed of LaSalle's Vice-Presidents and Controller, to discuss their individual areas of responsibility (CX 327I; Cornwell 1874–75).

42. Mr. Baker asked Mr. Marshall, LaSalle's Vice-President for Education to prepare a report setting forth planning suggestions for future operations (Marshall 1894). The report, entitled "A Plan to Make LaSalle Profitable Beyond 1980" (CX 426), was reviewed by Mr. Baker and portions of the plan were implemented shortly thereafter (Marshall 1894–95). Additionally, Mr. Marshall consulted with Mr. Baker respecting a suggestion for a new course offering in medical-dental reception (Marshall 1893).

43. The following are examples of transactions where Macmillan's approval was required prior to action by LaSalle:

(a) The purchase of any capital asset costing more than $100 (Barton 1806–07).

(b) A significant revision in an existing course (Barton 1807–09);

(c) Funding for development of new courses (Marshall 1953–54);

(d) Salaries for LaSalle personnel in excess of $20,000 (Barton 1821);

(e) Borrowing of money by LaSalle (Barton 1813);

(f) Expenditures for advertising in excess of budgeted amounts (Cornwell 1870–71).

(g) Personnel changes involving high-level LaSalle executives (Barton 1832); and

(h) Execution of consent agreements with state or federal agencies, when such [14]agreements concern LaSalle's operations (Barton 1818–19).

D. Macmillan's Financial Responsibility for LaSalle

44. Since 1973 Macmillan has guaranteed the financial stability

and performance of LaSalle to the NHSC, state and federal accrediting agencies (CX 326A, 329K, 380, 381A, 382). In many instances, such assurance has been accompanied by a copy of Macmillan's annual report (CX 326A, 329K, 380, 381A, 382).

45. The importance of Macmillan's financial resources to LaSalle was reflected in LaSalle's application to the NHSC for accreditation renewal. In response to the question, "What do you consider to be your single greatest asset which has been most responsible for your growth?" LaSalle replied, in part:

> . . . financial support from the parent corporation, Macmillan, Inc., America's largest educational/information/culture publishing congeneric.

(CX 281C, G; see also CX 425K). In the NHSC's summary of its accreditation committee findings, LaSalle was found to be "sheltered under the umbrella of the financially strong MacMillan, Inc." (CX 328I).

46. Macmillan established uniform accounting practices for itself and all of its subsidiaries (Barton 1815); its auditors, Deloitte, Haskins and Sells, audited Macmillan's books and those of every Macmillan subsidiary on a periodic basis. In those years when Deloitte, Haskins and Sells did not audit LaSalle's books, Macmillan's internal audit department conducted the audit (Barton 1815–16).

47. Macmillan filed a consolidated corporate income tax for all of its domestic subsidiaries and incorporated the financial statements submitted by LaSalle into its annual report and SEC filings (Barton 1816–17).

48. Macmillan established a common checking system in its name in Seattle, Washington, which was used by LaSalle and thirteen other subsidiaries to handle accounts payable (DeWerth 1844–45). LaSalle, which used the common checking system in the normal course of its business, submitted invoices for payment to the common accounts payable system (DeWerth 1844–[15]45). Macmillan issued the check to the vendor about two weeks later. LaSalle paid its vendors through the common checking system unless the check had to be issued in less than two weeks (DeWerth 1845). LaSalle used the Macmillan account to issue refunds to former LaSalle students (RX 688A, B).

49. Macmillan loaned money to LaSalle (Barton 1817; DeWerth 1843). LaSalle was not empowered to borrow money on its own behalf (Barton 1817). When LaSalle had an excess of cash, it loaned the sum to Macmillan and if LaSalle needed cash, it borrowed directly from

Macmillan. All Macmillan subsidiaries followed this practice (DeWerth 1843, 1850). No minimum amounts were involved in such transactions, which were set up on a demand arrangement, and ranged from a few thousand to several million dollars (DeWerth 1850).

E. Miscellaneous Indicia of Macmillan's Control over LaSalle

50. Employees of both Macmillan and LaSalle have often participated in the same benefit programs such as a pension plan (DeWerth 1848), a welfare benefits plan (RA 10), and a dental insurance plan (RA 11).

51. Macmillan and LaSalle shared computer facilities, which were located at LaSalle (Barton 1825).

52. LaSalle operated the Business Information Reference Service as part of its Successful Small Business program (CX 426NN). This service was basically identical to the Crowell Collier Reference Service, which was offered through a different subsidiary of Macmillan (CX 426NN), but Business Information Reference Service was operated by LaSalle (CX 426III) and used by LaSalle faculty members (CX 426KKK; see also CX 426JJJ).

53. The activity reports submitted by LaSalle executives to Robert Barton dealt with matters, such as, a lack of dental benefits booklets for LaSalle employees, a lost requisition for replacement of a secretary (CX 506D), plans for testing LaSalle radio advertisements using Macmillan air time credits (CX 550G), or minor changes in advertisements (CX 541).

54. Macmillan approval was required before LaSalle could discontinue marketing its courses through field sales representatives and make a major investment in a mail-order marketing program (Barton 1806–07).

55. Although LaSalle was responsible for establishing the compensation schedules for its sales representatives, Mr. Barton's prior approval was required (Barton 1826–27). [16]Significant changes in the sales commission structure also required approval by Macmillan (Barton 1806–07).

F. Macmillan's Power To Control the Practices of LaSalle

56. On March 23, 1977, Robert A. Barton, acting as President of Macmillan, sent a letter to the Indiana Private School Accrediting Commission, conveying Macmillan's guarantee, as LaSalle's corporate parent, for the full performance by LaSalle of its obligation to provide the educational services contemplated by LaSalle's contract

with each student previously or prospectively enrolled who remains in good standing (CX 383). The Board of Directors of Macmillan ratified Mr. Barton's letter in April 1977 (CX 384B).

57. Macmillan has the authority and power to direct the policies and practices of its subsidiary, LaSalle (Findings 14–56).

III. Promotion, Marketing, and Sale of LaSalle Correspondence Courses

A. In General

58. Respondents disseminated advertisements in various publications of general circulation in order to obtain leads for the sale of their correspondence courses (Comp. Par. 3; LaSalle Ans. Par. 3). These publications included *T. V. Guide, American Home, Cosmopolitan, Mademoiselle, Glamour, Decorating Ideas,* and group publications such as the Fawcett Detective Group, Secret Romance Group, and Complete Men's Group (CX 1–65).

59. Until March 31, 1979, respondents used a field sales force dealing directly with the public to sell and market their correspondence courses (Israel 1988, 1990; Letter of respondents' counsel, dated December 14, 1978).

60. LaSalle relied upon its nationwide advertising to develop a market for its courses. Attached to each advertisement was an inquiry card, on which prospective students indicated their name, address, and course of interest (CX 1-[17]65). The inquiry cards were converted into "blue leads" which contained the prospective student's name, address, and course of interest (CX 151U; RX 101C). The leads were distributed to sales representatives through their regional or district managers (CX 151H; RX 101C, 102D, 103D). Blue leads (RX 224) were the sales representatives' primary source for identifying prospective students (Werner 2795–97).

61. Sales representatives were also responsible for obtaining "personally developed" leads, referred to as "PD's" (CX 151V; RX 101C, 102D, 103D). Similarly, leads were developed through LaSalle's Goodwill Club (CX 151H, V; RX 101C) and through contacts with corporations (Werner 2797).

62. In addition to accepting applications submitted by its field sales force, LaSalle accepted enrollments through a mail-order procedure (CX 327UUUU-VVVV, 425X; Berry 2338–40; Brooks 2679; Miller 2922; Visser 2941). LaSalle had used a direct mail order sales solicitation program at sometime prior to 1977, which it discontinued because it was unsuccessful (CX 528B).

63. After receipt of an inquiry, detached from one of its advertise-

ments, LaSalle, in addition to preparing and distributing a blue lead card to its sales representatives, sent a brochure to the prospective student describing the course in which the student had expressed an interest (CX 151W, 327BBBBB). The brochures were accompanied by a cover letter informing the prospective student that a LaSalle sales representative would call on him personally (CX 101–08; 115–19; 151W, X, 167C). As a general rule, prospective students received such brochures in the mail prior to contact with the sales representative (CX 153MM).

1. Respondents' Field Sales Force

64. In the period 1975–1978, the LaSalle field force ranged from 1000 to 108 individuals; the sales force diminished toward the end of that period (Israel 1989; CX 327DDDDD). In 1975, about 500 of the sales representatives received at least one enrollment in any given week (CX 327DDDDD).

65. The LaSalle representatives were paid commissions for enrollments secured. The compensation schedule as set forth in the 1976 Representatives Manual was the following:

The three commission amounts paid are:

Enrollment commission – You will be paid $70.00 for each student you enroll whose application [18]is accepted and processed in the home office. This commission will be paid on all courses; there are no exceptions.

30-day service commission – You will be paid $25.00 for each 30-day callback you maké in person. The callback must be made on time, the student's tuition payment must be current and the Records Confirmation Slip must be received and processed by the home office on schedule.

PD enrollment commission – You are paid $25.00 for each PD enrollment which is paid to date at 90 days. This means the first three monthly payments must have been submitted on time.

66. The enrollment commission was received from the first payment remitted by the student. When a student did not pay the tuition agreed upon in the Retail Installment Contract, LaSalle would recover part or all of the commission already paid to the salesman under a "chargeback" or repayment of the commission (CX 151DDD).

67. If a student remained enrolled in a course for more than 90 days and his payments were current at the end of that period, the representative would not lose any of his commission if the student dropped out at that point (RX 103G; Werner 2822).

68. The number of enrollments was a major factor in a sales representatives' earnings (Werner 2823–24).

69. In 1971, LaSalle instituted a Graduation Bonus Plan under which a representative received a 50 percent bonus for all enrollees who graduated. This program, however, was discontinued in 1975 (CX 327FFFFFF; Werner 2821–22). Respondent also had a quality bonus to reward representatives who secured better studying and paying students (CX 327FFFFFF).

70. LaSalle representatives were expected to maintain a high conversion rate on leads generated by advertising because [19]they represented a major expense item. Respondents informed their representatives "We expect new representatives to sign up at least one person in ten; some experienced representatives sign up two or three out of ten" (CX 151H).

71. LaSalle's representatives were subject to immediate termination for cause such as dishonesty, misconduct and misrepresentation. In addition, representatives, except under unusual circumstances, were terminated if they failed to submit at least one application in a 30-day period (CX 327GGGGG).

72. The turnover rate for respondents' sales representatives was high. Approximately 75 percent of the active sales representatives were employed less than one year (CX 328, Report of Accrediting Examining Committee, National Home Study Council submitted December 2, 1975).

73. LaSalle stopped sending leads to its representatives in December 1978. It continued to process and accept enrollments obtained by representatives without leads until March 31, 1979. On that date, the remaining representatives were terminated (CX 327UUUU; Marshall 1907; Werner 2793; Finding 59).

B. The Sales Presentation

74. Generally, sales representatives established initial contact

with the student by telephone (CX 514B; Mull 329–30; Shulock 362; Muhar 446; Waller 657–58; Mastrangelo 752; Wilmot 795–96; Lapeer 837; Nehls 864; Kammer 887–88; Reed 1571; Deet 1686; Patrone 1754; Wilson 3271; Sellers 3258–59; Kohlmyer 3338; Ostland 3489; Burritt 3625–26).

75. LaSalle representatives did not enroll applicants. Enrollment was done by the Home Office. Sales representatives were instructed to interview applicants to see if they qualified in terms of having the time, money, and motivation to study and succeed, fill out an enrollment contract and secure a down payment (CX 168R).

76. LaSalle's sales representatives were trained and instructed to use a standard sales presentation "The Qualifying Interview" (CX 151K, 153F, 154, 168D). "Practically the entire interview is a readoff from printed materials plus a few passages to be memorized" (CX 153C). The sales presentation did not require a knowledge of the subject matter of the courses (CX 328U).

77. The LaSalle sales representatives were instructed that:

The Qualifying Interview is a field proven technique which lets you take control of the interview and keep control of it. The [20]qualifying format insures an orderly step by step presentation that takes you from the applicant's door, through the presentation and brings you to filling out the enrollment contract and Congratulatory Talk. The LaSalle Method enables you to eliminate costly digressions or sidetracks and answers most of the applicant's questions before they're asked.

Through the use of a printed Qualification Questionnaire and an all-course Visual you can quickly learn how to conduct a Qualifying Interview. With practice you'll deliver it skillfully each and every time.

. . . Each step is vital to the success of your presentation. Failure to adhere to this method usually results in poor quality enrollments. To maximize your time and efforts learn each step in the Qualifying Interview well.

(CX 168D)

78. LaSalle's standard sales presentation consisted of five parts: prescreening or greeting the prospect, intensive qualification, visual presentation, the close, and the after sale or congratulatory talk (CX 154, 168D; RX 101D, 102D, 103D, 133D).

79. Respondents' sales representatives were instructed to memorize the following pre-screening talk:

Mr. Miller, in the short time I have to spend with you, I'd like to speak with both you and Mrs. Miller. May we be seated at a table please?

As I said, Mr. & Mrs. Miller, I'm the local representative of LaSalle Extension University. I'm here in response to your inquiry about self-improvement. To begin, I want to be sure that we have a program that is right for you, Mr. Miller, and that you

are right for the program. As a leading [21]correspondence school, LaSalle will only accept students who can benefit from its program of study. To determine whether you can benefit, Mr. Miller, we'll be discussing your reasons for wanting more education and your desire and ability to study and succeed.

(CX 168D)

The purpose of the pre-screening talk was to put the student on notice that he had to qualify for admission to the LaSalle Program and that acceptance was not automatic (CX 153L; 168E).

80. The heart of the sales presentation was the "intensive qualification". This part of the presentation was conducted by means of LaSalle's "Confidential Qualification Questionnaire." The purpose of the questionnaire was to help the sales representative discover the applicant's needs, character, capabilities, financial means, and whether the applicant qualified for enrollment (CX 168I; Wilmot 797–08, 803–08). Sales representatives were further instructed that "The QQ [Qualifications Questionnaire] is a powerful tool in the hands of a person [respondent's salesman] who has learned to use it for all its worth" (CX 153 O). The Qualification Questionnaire, according to respondents' directions could also be used to meet "objections and stalls what may come up later at the close" (CX 153 O).

81. After the intensive qualification, the sales representative used a visual presentation to describe the course content, the advantages of home study and LaSalle (Wilmot 810–14; CX 153F, MM, NN, 157, 168R). The brochure received by the prospective student prior to the sales presentation was used by LaSalle's representatives to supplement the material in their sales binder (CX 153MM, 157; Shulock 373–76).

82. The next step of the sales presentation was the "close" (CX 153QQ). LaSalle instructed the sales representative to use an "assumptive close" namely assume the prospect is ready to fill out the enrollment application, sign a contract, and make a down payment (CX 153SS). If a prospect appeared hesitant at this point, the sales representative was to go back to key questions and answers elicited in the "intensive qualification" in order to meet objections (CX 153BBB–CCC).

83. After concluding the sale, LaSalle's sales representatives were instructed to give an after sales talk congratulating the prospect on his decision "to reinforce the sale" "And help keep it sold" (CX 153EEE, 154D, U, 168Q). The student was told he had three obligations: to study and succeed, to provide his family with a better

way of life, and to submit his tuition payment on time (CX 153EEE, 168R). [22]

1. The Retail Installment Contract

84. The retail installment contract or field enrollment form/contract used by LaSalle was a two-part document. The field representatives were instructed to leave a carbon copy with the prospective student. In the case of a mail order enrollment, a duplicate of the original was returned to the student upon enrollment acceptance (CX 327VVVV).

85. LaSalle's "Federal" retail installment contract incorporated federal, Illinois, and NHSC requirements and LaSalle policies. It was used, according to respondents, where those requirements were more to the student's benefit than the applicable state regulations. The other contract forms bearing the names of particular states were used because the regulation of that state required some specific language or because the state regulations, according to respondents, were more beneficial to the student than the federal regulation (CX 327VVVV).

86. The mail order forms complied with the regulations of the State of Illinois, where LaSalle was domiciled (CX 327VVVV).

87. The "Federal" form of the Retail Installment Contract was the one most widely used (Martins 2668).

IV. Representations Made by LaSalle in Marketing Its Course

A. Success through LaSalle Theme

88. The major theme that permeated LaSalle's communications and representations to the public was the potential for success generated through completing a LaSalle course—the promise of higher salaries and future opportunities. This success through LaSalle theme was repeatedly expressed in LaSalle's advertising, which consisted of both combination advertisements and advertisements focusing on individual courses, its course literature, its brochures, and orally by its sales representatives.

89. Respondents' advertisements relied heavily on endorsements by satisfied LaSalle graduates to convey the success through LaSalle theme (CX 8A, 32, 559D, 577). These testimonials created the impression that such success was ordinary and typical of LaSalle graduates. [23]

90. LaSalle's print advertisements frequently covered not only individual courses, but a number of courses (CX 3–5, 10–25, 34–46,

116, 557). When testimonials were used in conjunction with combination ads, they conveyed the impression that the reader could be as successful as the person in the testimonials by enrolling in any one of the courses featured in the combination ad.

91. In combination with representations that the LaSalle diploma was a "recognized" or "useful credential" and that the diploma was evidence that a graduate of a LaSalle course had been "thoroughly prepared" by "one of America's most respected schools" (CX 101I, S, 103I, 104I, S, 105M), the testimonials created the impression that the LaSalle graduate needed no further training to enter the field of his choice.

B. Interior Decorating

92. LaSalle's advertisements regarding their complete interior decorating course appealed to women to put their "Love for decorating into a dream career" (CX 6B, 8A). Reiterating the basic theme of success through LaSalle, LaSalle advertisements billed interior decorating as "a high-income field where a woman is in her glory. There is a good demand for decorating services and opportunities are abundant" (CX 29).

1. LaSalle Represented There Was a Need or Demand for LaSalle Graduates in the Field of Interior Decorating

93. LaSalle represented that there was a demand for LaSalle graduates in the field of interior decorating. LaSalle advertisements contained such statements as:

> There is a good demand for decorating services and opportunities are abundant. . . A tremendously expanded field (CX 29).

94. Representations such as these coupled with statements such as:

> I have now opened a studio . . . and I am already getting demands for interior decorating services (CX 711A). [24]

> LaSalle's interior decorating course gives you complete, up-to-date instruction at home (CX 6B, 32).

> The LaSalle course in Interior Decorating has been prepared to give you practical, complete and up-to-date preparation for this exciting career (CX 29).

which created the impression that the LaSalle graduate was a trained interior decorator, resulted in the impression that there was

a need or demand for LaSalle graduates in the field of interior decorating.

95. After the initial contact with LaSalle through its advertising, the prospective student received a course brochure which further outlined the benefits of the particular LaSalle course. "Your Future in Interior Decorating" was the title of the two brochures used to illustrate the success possible with LaSalle's interior decorating course (CX 101, 104). A headline in CX 101C characterized interior decorating as "a vastly expanded field where you can turn your creativity into profit." The text of both brochures represented that there was an increasing need or demand for interior decorators.

> Opportunities for trained decorators are increasing each year. It used to be that only the wealthy employed decorators. That's no longer true. Large numbers of average homemakers now rely on the services of decorators. . . .
>
> Decorators today are busy in many areas besides homes. Their talents are employed in decorating hotel rooms, business offices, building lobbies, hospitals and many other interesting places. Some decorators operate their own businesses; others work in major stores, showrooms and design studios. (CX 101C)
>
> Opportunities for trained decorators are increasing each year. Their talents are employed in decorating hotel rooms, business [25]offices, building lobbies, hospitals and many other interesting places. Some decorators operate their own businesses; others work in major stores, showrooms and design studios. (CX 104C)

96. The impression was created in the first few pages of the brochure that there was a demand for interior decorators; the remainder of the brochure, dedicated to showing the prospective student how LaSalle trains him to be an interior decorator, created the impression that the LaSalle trained graduate would be qualified to enter this expanding field.

> How LaSalle training prepares you for a career as an Interior Decorator (CX 101I; see also CX 104I).
>
> If you want to start an exciting career as an interior decorator, LaSalle will prepare you for it in a home study program that is both practical and delightful (CX 101M).

These representations in conjunction with and as an integral part of the LaSalle presentation, which included the representations that there was a substantial need or demand for interior decorators, created the impression that there was a substantial need or demand for LaSalle graduates in the field of interior decorating.

97. LaSalle's sales representatives were instructed to repeat the employment opportunity claims made in LaSalle's brochures; they were not to make any representations of their own contrivance (RX

102G, 128B). Student testimony indicates that such claims were repeated.

Q. Did she describe what career opportunities might be available to you in interior decorating?
A. Yes.
Q. What did she say?
A. That you could go into many areas, such as working for a furniture [26]store, become a buyer for department stores, an interior decorator, whatever appealed to you (Haselden 2196).

98. The continued repetition in LaSalle's advertisements, brochures, and orally by its sales representatives of the need or demand for interior decorators coupled with the representation that the LaSalle course offered complete training had the capacity to convey to prospective students that there was a need or demand for LaSalle interior decorating graduates.

2. LaSalle Represented That Its Interior Decorating Graduates Would Increase Their Earnings

99. In a number of ways LaSalle's advertisements created the impression that students completing respondent's correspondence courses would receive high wages or salaries from employment as interior decorators. The advertisements boldly stated that whatever your assignment as an interior decorator "you'll be well paid for it" (CX 6A, 8A) and "a decorator earns good money for work she enjoys" (CX 32). Testimonials from graduates of the LaSalle course were also included in some advertisements and appeared to substantiate the success through LaSalle theme. These graduates attested to increased earning power:

Mrs. Faye C. Haynie
Benton, Kentucky

> Now I feel like Onassis when I compare my earnings with what I used to make (CX 559D).
> I feel rich when I compare my earnings with what I once used to earn (CX 8A, 32).

Lucy Kovesi, Town Gallery
New York, New York

> LaSalle training helped me develop my own successful gallery of art for decoration. I've enjoyed increased earnings and prestige (CX 6B, 7B, 8B). [27]

In other advertisements successful graduates were used as examples of the increased earnings made possible by a LaSalle diploma in

interior decorating. Mrs. Faye C. Haynie's success story of markedly increased earnings is featured repeatedly in advertisements (CX 6A, 7A–B, 8A–B, 30A–B, 31, 740). Other examples were used such as Susan Wilson, Opelika, Alabama (CX 33) and Sara P. Hendren, Indianapolis, Indiana (CX 711B) whose salaries were reported as having doubled.

100. LaSalle's advertisements implied a parallel between the individual in the success story and the individual reading the advertisement. Sometimes the parallel was expressly drawn as in CX 711B "These people have a lot in common with you" referring to the success story of Mrs. Haynie and that of Sara P. Hendren. Although in some instances there was language in the text of the advertisement which proposed to limit the scope of these success stories, the limiting language did not cancel out the effects of the testimonials which led the prospective student to believe that such success was ordinary and typical of LaSalle graduates.

101. For example in CX 33, which consisted of a number of testimonials from LaSalle interior decorating graduates from across the country, the caveat "An exceptional case, of course, but it does show how well some creative women can do when they develop their talents" is lost amid numerous testimonials and headlines proclaiming "The success of LaSalle graduates."

102. The course brochures used by LaSalle reiterated the promise of higher earnings:

A vastly expanded field where you can turn your creativity into profit (CX 101C).

103. The brochures also utilized testimonials from successful LaSalle graduates (CX 101R, 104R).

Your Interior Decorating course has given me many, many enjoyable and profitable hours.

Lorraine Howland
Regina, Saskatchewan
(7/11/77)

As an Interior Designer my salary has more than doubled. [28]

Janiene Church
Lakeland, Florida
(8/27/76)

(CX 104R)

My salary has doubled.

Linda Rae Kronberger

Sturgeon Bay, Wisc.

My interior decorating course enabled me to get a terrific new position in a furniture showroom and most importantly, my salary has doubled.

Deborah A. Cosgrave
Reading, Pa.

. . . and my salary has more than doubled since I started my new career.

Susan C. Wilson
Opelika, Ala.

(CX 101R)

104. Ms. Wilson's success story was the subject of a double page spread in CX 104E. Her successful climb from secretary to interior decorator at "twice former salary" is featured under her picture and the headline "How LaSalle helped change the life of Susan Wilson" (CX 104E).

105. Although the statement at the end of Susan Wilson's story characterized her as an exceptional case, the overall impression conveyed was that similar success could be expected by the reader after LaSalle training (CX 104E). Even the statement that was to limit her success to that of an exceptional individual concluded with:

but it does show how far *your* natural talents can take *you* with the help of LaSalle training (emphasis added) (CX 104E). [29]

106. The promise of monetary success which was awakened by LaSalle's written materials was further stimulated by its sales representatives in the qualifying interview.

J: OK. Let's take that complacent chap again. Mr. Miller, are you satisfied with your present earnings?
Mr. M: Oh, we're getting along pretty good.
J: You're completely satisfied? There isn't anything you'd buy or do if you had more money?
Mr. M: Oh, sure. You can always find places to spend money.
J: Mrs. Miller, are you satisfied with his income?
Mrs. M: Oh, he provides for us pretty well.
J: There isn't anything you'd do differently if you had more money?
Mrs. M: Well, there's probably all kinds of things we'd do.
J: For instance?
Mrs. M: Well, we'd get a better house.
Mr. M: After we'd get a new car.
Mrs. M: We'd take a real vacation.
J: These are all things you'd be able to do when you get started in your career in accounting.
Mr. M: We hope so.

* * * * * * *

N: What about this next question? What would you like to earn five years from now?

J: Well, the first thing to realize about that question is that the average person you're talking to never thinks much beyond next month or next Christmas or the date he feels [30]he'll be due for his next pay increase. He's almost never given thoughts to what he wants to be making 5 years from now.

N: So you may have to lead him. You have to be prepared to suggest a figure if he doesn't come up with one.

J: Right. No matter what he's earning today, I get him to set a target figure that he'll agree he can't possibly reach through normal advancement in his present situation. But a figure that is realistic in relation to whatever course it is he wrote in about.

N: Setting the stage for the next question—What can you do about it?

J: And if he fumbles around with the answer to that one—I simply hammer home the obvious. That the only way he can possibly get there from here is by self-employment through further education (CX 153BB-DD).

107. Some students who testified about the qualifying interview stated that the representative represented the student would be entering a high paying field:

A. Specifically, I can't tell you, because I can't remember that far back. Approximately what went on was basically that it was a good course, that after completing the course, you can get a good paying job, and you would be a qualified interior decorator, and you'd receive a certificate from them stating so.

Q. Do you recall anything else that was said at the sales presentation?

A. He brought up the fact of a friend being in real estate and decided to go into interior decorating because it was such a good paying area (Mastrangelo 753).

A. He asked me where I was working, and informed me that I would—by taking this course, I would be able to increase my [31]salary or my earnings far more than what I had been getting (Muhar 448-49).

108. The overall impression that was created was that the LaSalle interior decorating graduate would be able to command a high salary or high wages.

3. LaSalle Represented That Its Graduates Would Be Qualified To Enter the Field of Interior Decorating with No Further Training

109. LaSalle created the impression that completion of the LaSalle interior decorating course qualified the student to secure employment in the field without further training or experience.

110. Advertisements stated that "the LaSalle course in interior decorating gives you *complete* up-to-date instruction at home" (CX 6B, 7B, 30B, 31, 32) (emphasis added) or that "the LaSalle course in Interior Decorating has been prepared to give you practical, complete and up-to-date preparation for this exciting modern career" (CX 29).

111. Aside from stating that LaSalle's course was up-to-date, practical and complete, the advertisements represented, directly and through the use of testimonials, that LaSalle had prepared many other women for successful interior decorating careers.

LaSalle training has helped many other women become successful decorators. LaSalle could help you do it, too.

For a beginning, you may prefer a position in a decorating studio, home furnishing gallery, or smart department store. With experience, you'll have every opportunity to build an independent business of your own (CX 6A).

112. In conjunction with Mrs. Faye C. Haynie's testimonial and a number of other testimonials, advertisement CX 7A–B proclaimed that: [32]

They turned their love for decorating into a dream career. Perhaps you can too. Free Booklet tells how LaSalle helps women train at home in spare time for interior decorating.

113. The featured testimonials showed how LaSalle graduates had achieved successful employment in the interior decorating field with LaSalle training.

Thanks to my LaSalle training I became the interior decorator for a leading department store.

Mrs. Joan Koston
Mentor, Ohio

(CX 7B)

114. The combination in LaSalle's advertisements of the success stories featured in the testimonials, the claims of complete, up-to-date training, and the representations to the effect that you, the reader, would be able to turn your love for decorating into a dream career conveyed the impression that a graduate of LaSalle's interior decorating course would be qualified to obtain employment in the field of interior decorating without further training.

115. LaSalle's course brochure continued the impression that the graduate would be fully qualified for employment.

How LaSalle training prepares you for a career as an Interior Decorator (CX 101I; see also CX 104I).

116. Even the course objectives listed in the brochure gave the impression that the LaSalle graduate would be qualified as an interior decorator.

COURSE OBJECTIVE: The Interior Decorating course is designed to give the student

practical knowledge and skills which may be applied commercially as well as personally in his or her own home. [33]

Upon successful completion of the 21-lesson course, the graduate will be able to apply sound decorating principles to problems ranging from simple furniture arrangement or window treatments to the complete design of one or more rooms in private homes or commercial establishments (CX 101N, 104N).

117. Part of the success through LaSalle sales pitch used by LaSalle's sales representatives implied that upon graduation from LaSalle the student could successfully seek employment as an interior decorator. In accordance with the qualifying interview script the sales representative would emphasize LaSalle's "practical program for your career advancement" with a school that "has been a leader in home study for over 60 years" (CX 153NN). The representative was to state:

. . . LaSalle supplies everything you need to prepare for a successful career (CX 153NN).

118. LaSalle's sales force represented that the LaSalle graduate was qualified for a career as an interior decorator.

Q. Do you recall what, if anything, the salesman said about your prospects of finding a job upon completion of the course?

A. Well, he said that after I had completed the course, and when I got my diploma, that I, as an interior designer, when I went out and looked for a job, they are not asking for experience, they are asking for qualified interior designers.

Q. Did he state whether LaSalle—graduation from LaSalle interior decorating course made one a qualified interior designer?

A. Yes, he did.

Q. What did he say? [34]

A. He said exactly what I had said, that by having my diploma, I would be a qualified interior designer. (Muhar 450).

Q. Did she describe what career opportunities might be available to you in interior decorating?

A. Yes.

Q. What did she say?

A. That you could go into many areas, such as working for a furniture store, become a buyer for department stores, an interior decorator, whatever appealed to you (Haselden 2196).

119. Student testimony reveals that the impression conveyed by the sales representatives was that the LaSalle graduate could get a job.

Q. What did you think your chances were of obtaining a job after you completed the LaSalle interior decorating course?

* * * * * * *

A. I thought they'd be very good.
Q. What was the basis of your—that impression?
A. Well, I assumed that by taking this course and getting a diploma, that I would have a good chance to go out and get a job (Muhar 451–52)

4. Expert Opinion as to LaSalle's Training and the Employability of LaSalle Interior Decorating Graduates

120. In its advertisements, brochures and through its sales representatives, LaSalle represented that its interior [35]decorating graduates would be qualified for employment in the field.

121. An interior decorator has been defined as someone who does primarily cosmetic work on interiors as opposed to an interior designer who is concerned with designing or remodeling the functional architectural aspects of interiors. Some interior decorators do work with some basic functional aspects of interiors.[3]

122. Although these distinctions are made by some, others consider the difference between the two as merely a matter of semantics (Genis 3400–01; see also Walker 488–89). It is clear, however, that whether termed designers or decorators there are those who function at various levels of sophistication in the interior decorating field.[4]

123. Respondents represented through their advertisement, brochures, and sales representatives that a LaSalle graduate [36]would be qualified to enter the field of interior decorating with no further training (Findings 109–119). Advertisements stated that "the LaSalle course in Interior Decorating has been prepared to give you practical, complete and up-to-date preparation for this exciting modern career" (CX 29).

124. The course objectives outlined in the brochure and LaSalle's self-evaluative report for the NHSC indicated that the LaSalle graduate should, upon completion of the course, be able to do residential or commercial designing as a decorating consultant or in his own interior decorating service.

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[3] Professor Rankin has defined an interior decorator as:

> (implying) coordination and completion of an interior space in terms of general visual and general functional aspects (Rankin 1304).

as opposed to:

> The term interior designer (which) generally implies the establishment of the square footage or the definition of the space, the review and organization of the peculiarities or functions of a space, the selection of the specification, materials to complete that interior, and the selection of the components required to finish that interior space or the design, selection or specification of any components that cannot be purchased but must be custom made and supplied for that interior space (Rankin 1304).

[4] Arline Genis' description of a decorator working at an advanced level seems to correlate with Nancy Walker's and Professor Richard Rankin's description of an interior designer (Genis 3402–03; Rankin 1304; Walker 488–92).

COURSE OBJECTIVE: The Interior Decorating course is designed to give the student practical knowledge and skills which may be applied commercially as a career as well as personally in his or her own home.

The course provides a basic knowledge in: the use of colors in decorating, planning room proportions, fabric selection and use, choosing the proper wall covering, the decorative aspects of lighting, the use of accessories for accent, identifying and selecting the proper periods of furniture as well as how to establish a decorating business as a career.

Upon successful completion of the 21-lesson course, the graduate will be able to apply sound decorating principles to problems ranging from simple furniture arrangement or window treatments to the complete design of one or more rooms in private homes or commercial establishments (CX 101N, 104N).

125. The report to the NHSC, while not a representation made to consumers, serves as a useful aid in construing the advertised course objectives. In much the same language used in the brochure it states:

3. Expected Outcome.

Upon successful completion of this course, the graduate will be able to apply sound decorating principles to problems [37]ranging from simple furniture arrangement or window treatment to the complete design of one or more rooms in private homes or commercial establishments. The graduate may begin a career as a decorating consultant advising on the purchase of carpeting, furniture or other home furnishings in department stores or specialty stores. Alternatively, graduates should be able to establish and operate their own interior decorating services, or, if they prefer, they can enrich their lives by the pleasure of decorating their own homes (CX 327V).

126. The course objectives as stated are ambiguous. At one point, the objectives state that "the course provides basic knowledge" at another point they maintain that "the graduate will be able to apply sound decorating principles . . . to the complete design of one or more rooms in private homes or commercial establishments," from the latter one can infer that the LaSalle graduate will be able to work at the advanced level (CX 101N, 104N).

127. The net impression created by LaSalle's representations to the public was that the interior decorating graduate could qualify for employment on the advanced level.

128. In contrast to LaSalle's representations, the experts agreed that while LaSalle offered training in the basics of interior decorating, it did not adequately prepare the ordinary and typical individual to be an advanced level interior decorator (CX 1032; Genis 3427–28, 3477; Walker 527–28; Rankin 1336–39). The ability to work on advanced levels depends on natural ability and experience, as well as formal training. Many of the skills received in the field cannot be learned from a book or in the classroom (CX 1032; Genis 3408, 3416, 3424–28; Rankin 1340). While some graduates of the LaSalle

program were able to accomplish the vocational objective of obtaining employment in the field of interior decorating with department stores, furniture or home furnishings stores, decorating studios and individual decorators, the ordinary and typical LaSalle could not perform in the field at more than a basic level (Rankin 1338–40; Brooks 2676; Murphy 2761; Wright 2878–80; Kohlmyer 3336; Genis 3407–08, 3437–39).

129. LaSalle also represented in its advertisements and in the course objectives outlined in its brochures and report to the NHSC that one of the options open to the LaSalle graduate would be to establish his own interior decorating business (Finding 124). In order to function as an independent interior [38]decorator an individual would have to perform on an advanced level (CX 1032; Genis 3401–07, 3437–39, 3445–82; Rankin 1335–40, 1345, 1347). Since LaSalle's course did not prepare its graduates to function beyond the basic level, it was false and misleading to represent that the ordinary graduate could open his own interior decorating business.

130. To the extent that LaSalle represented its typical and ordinary graduate was qualified for advanced level positions, LaSalle's representations were false and misleading.

131. Since the ordinary and typical interior decorating graduate would be unable to open his own decorating service or obtain employment beyond the basic level, representation made by LaSalle that there was a demand for LaSalle graduates and that they could expect a substantial increase in income were false and misleading.

B. Computer Programming

132. LaSalle represented that computer programming was an opportunity field—a high paying, rewarding career (CX 4A, 8A). They also represented that success in the field of computer programming could be attained by enrolling with LaSalle (CX 3, 4A, 5A).

1. LaSalle Represented That There Was a Need or Demand for LaSalle Graduates in the Field of Computer Programming

133. Respondents' advertising, through statements such as the following, had the tendency and capacity to create the impression that a substantial demand existed for computer programmers in general and for graduates of LaSalle's basic computer programming course in particular.

Grow with the future. Train at home for one of these

6 technical fields

For over sixty years LaSalle has been helping ambitious men start new and profitable careers. We can help you too. [39]

* * * * * * *

For a prestige career why not get into computer programming (CX 3).

Which one of these 6 opportunity fields is right for you?

First pick a growth field where you can move ahead fast. Second prepare with the right training—LaSalle training.

* * * * * * *

For good pay and prestige why not get into computer programming (CX 4A; see also CX 5A).

COMPUTER PROGRAMMING

Prestige career in a field that offers big opportunities (CX 4A).

134. The impression created in LaSalle's advertising was reinforced in its course brochures. In addition to outlining the contents of the LaSalle Basic Computer Programming course, respondents' course brochure for computer programming contained the following statements about the need or demand for computer programmers:

Why Does the Computer Field Attract So Many Ambitious Men and Women?

As the economy grows, the opportunities for the trained computer operator continue to increase. . . .

* * * * * * *

It takes training and experience to handle the programming assignments the business world turns over to the [40]computer. LaSalle can provide you with basic computer programming training. If you combine this training with on-the-job experience, you will discover what interesting work computer programming can be (CX 103C).

* * * * * * *

Convenient and Practical Training For You

Now in your spare time at home, LaSalle teaches you the special techniques for developing and writing programs for business computer operations.

You'll find learning Basic Computer Programming with LaSalle an ideal way to prepare for the computer age (CX 103E).

The above representation (CX 103E) was used in conjunction with a graph citing U.S. Dept. of Labor Statistics and showing a rise in the number programmers employed from 80,000 in 1965 to 186,000 in

1972 (CX 103E; see also, CX 106E comparing employment figures of 80,000 for 1965 and 223,000 for 1975 in conjunction with the same textual representation).

135. Statements such as the foregoing had the tendency and capacity to create and reinforce the impression initiated in LaSalle's advertisements that there was a substantial need or demand for computer programmers in general and for graduates of LaSalle's computer programming course in particular.

136. The theme that there is a substantial demand for graduates of LaSalle's computer programming course was continued in the sales presentation with the visual supplied to salesmen (CX 157LL).

137. A LaSalle sales representative stated that "LaSalle's placement record was excellent and if [the student] did all the home work and like that and got good grades on it, [the student] should have no problem getting into the field" (Mull 337; see also Mull 333–34).

138. Sales representatives were instructed to repeat the employment claims made in the course brochures (RX 102G, 128B). [41]

139. The repetition in LaSalle's advertisements, brochures, and orally by its sales representatives had the tendency and capacity to create the impression that a substantial need or demand existed for graduates of LaSalle's basic computer programming course.

2. LaSalle Represented That Its Computer Programming Graduates Would Increase Their Earnings

140. LaSalle's advertisements used student testimonials and text written by LaSalle to convey the impression that LaSalle computer programming graduates could expect to receive high wages or salaries. Consistent with the success through LaSalle theme, the advertisements for computer programming posed questions such as:

What does it take to earn higher pay? (CX 5A)

What does it take to command a much larger salary than you now earn? (CX 4A)

HAVE YOU SEEN THIS COUPON BEFORE?

It has helped to start many men and women on the road to higher pay. Just looking at it won't get you anything . . . but putting it in the mail may change your whole future! (CX 11)

LaSalle training was presented as the answer to financial success.

141. LaSalle made affirmative statements about the ability of computer programmers to earn good salaries. In some instances, computer programming was presented as one of a number of fields which offered the opportunity for financial success.

Choose from 20 growth fields that offer opportunities to earn more money (CX 12A)

For good pay and prestige why not get into computer programming (CX 4A). [42]

142. LaSalle used student testimonials to drive home the success in computer programming through LaSalle theme. The testimonials featured in CX 4 and 5 showed two LaSalle graduates who succeeded in changing their lives and increasing their salaries after completing a LaSalle course. The advertisements encouraged the prospective student to send for a free booklet that might "change your future" (CX 4B, 5B); the implied representation was that taking the LaSalle course would change the prospective student's life like it had changed the lives of the individuals featured in the testimonials.

143. Statements such as:

More than 2,000,000 men and women have enrolled for success with LaSalle Extension University (in bold print)

in close conjunction with testimonials from successful LaSalle graduates stating:

My salary has quadrupled since starting the course.

Thanks to my LaSalle training . . . my salary has more than doubled.

I now earn three and a half times my former pay (CX 17; 19B).

had the tendency and capacity to create the impression that the typical and ordinary graduate of the LaSalle basic programming course would be likely to experience the vocational and financial success promised in the advertisement (CX 17).[5]

144. In a similar manner LaSalle's computer programming course brochures, which included the testimonial of Clifford H. Smith of Great Falls, Montana, conveyed the [43]impression that financial success was attainable with the LaSalle computer programming course.

As a result of taking the Computer Programming course, I was promoted from the parts department of my company to the computer department . . . salary up 35% (CX 103Q, 106Q).

145. The promise of monetary success was repeatedly reinforced in LaSalle's advertising, course brochures and in the standard sales presentation (Finding 106). The net impression created was that the LaSalle computer programming graduate would be entering a high paying field.

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[5] CX 17 is a combination advertisement featuring the computer programming course among others.

3. LaSalle Represented That Its Graduates Would Be Qualified To Enter the Field of Computer Programming with No Prior Experience or Further Training

146. LaSalle's advertisements implied that completion of their correspondence course without more qualified the student to enter the field of computer programming.

If you're determined to move ahead in your field of interest, LaSalle will give you the training you need for a good start (CX 4B).

What does it take to command a much larger salary. . . First pick a growth field where you can move ahead fast. Second prepare with the right training—LaSalle training (CX 6A).

LaSalle's advertisements stated that no prior experience or technical background was a prerequisite for the LaSalle course.

For a prestige career why not get into computer programming? All it takes to start training is a high [44]school education and a logical mind. No technical background is required (CX 3).

. . . All it takes to start training is a high school education and a logical mind. No technical background required. . . . (CX 4A).

The combination of these representations had the tendency to create the impression that no prior experience or further training was required to enter field of computer programming.

147. The LaSalle computer programming brochure reiterated the theme that successful employment in computer programming was attainable with LaSalle alone.

The LaSalle diploma is a useful credential because it testifies that you have been *thoroughly prepared* for your work in basic computer programming (CX 103I; see also CX 106I) (emphasis added).

* * * * * * *

How Can You Prepare Yourself To Enter This Rewarding Field?

LaSalle may be the answer for you—it has been for countless others (CX 103F–G, 106F–G).

This training combined with the graduate's personal ability, prepares him to enter the field as a Computer Programming Trainee . . . (CX 103F, 106F).

148. The course objectives set forth in the brochures furnished to prospective students described the basic computer programming course as follows:

The Basic Computer Programming course is designed to provide the student with a

knowledge of the fundamental concepts [45]in computer programming and introduce him to the organization and function of a data processing department.

The successful graduate will have completed this 21 lesson course with instruction in the basic principles on which computers work; the use of flowcharts to divide a problem into its smallest parts; the use of flowchart information to write an actual computer program; the common programming languages with development of a working knowledge in the COBOL language; the use of program and system controls and how they relate to the "hardware" controls built into the equipment; the writing of actual programs for the latest model computers. This training, combined with the graduate's personal ability, prepares him to enter the field as a Computer Programming Trainee performing such functions as converting flowcharts from rough to finished form, coding the flowcharts into COBOL language, and making minor changes in existing programs. Of course, no reputable school can guarantee future employment to a prospective student. But once you complete the LaSalle program, you will have an advantage over the untrained people with similar educational backgrounds who are trying to get into this rewarding field (CX 103F, 106F)

149. Respondents course objectives, as set forth in the brochures, may be summarized as follows:

Students would learn to use a flowchart to divide a problem into its smallest parts.

Students would learn the use of flowchart information to write an actual computer program.

Students would develop a working knowledge of COBOL.

Students would learn the writing of actual computer programs for the latest model computers. [46]

Students would learn to convert flowcharts from rough to finished form.

Students would learn to code flowcharts into COBOL.

Students would learn to make minor changes in existing programs.

150. Respondents through their course brochures represented that graduates of its basic computer programming course would be qualified to enter the field as computer programming trainee through the acquisition of certain skills (CX 103F, 106F).

151. Phrases in the respondents' brochure's description of the course objective such as:

The successful graduate will have completed this 21 lesson course with instruction in . . . . the use of flowchart information to write an actual computer program; . . . the writing of actual programs for the latest model computers . . . . (CX 103F)

had the capacity and tendency to create the impression that the

graduate of LaSalle's course would be able to write "actual" computer programs without further training.[6]

152. LaSalle further represented that its students could achieve the course objectives without access to a computer, "YOU DON'T NEED A COMPUTER TO LEARN COMPUTER PROGRAMMING" (CX 103G, 106G).

153. LaSalle's representatives reinforced the impression created in the advertisements and course brochures that the LaSalle graduate would be qualified to enter the field as a computer programmer trainee without prior experience [47]or further training. In accordance with the qualifying interview script, the sales representative was to state:

. . . LaSalle supplies everything you need to prepare for a successful career (CX 153NN).

The sales visual supplied to representatives for use with prospective students during the sales presentation included the following statement:

LaSalle supplies the training to acquire new skills, earn a college degree or start a new career (CX 157G).

154. The impression created by the advertising, brochures, and sales presentations in connection with LaSalle's computer programming course was that LaSalle offered complete training which would qualify its graduates to enter the field as computer programmer trainees.

4. Expert Opinion As To LaSalle's Training And The Employability Of LaSalle Computer Programming Graduates

155. Computer programming is the art of writing a set of instructions for a computer to do a specific job (Hamblen 1192).

156. A computer programmer trainee is an individual, generally on a probationary appointment, who will work under the supervision of programmers and analysts, as part of a team, for the purpose of writing computer programs (Engel 927). It is the entry level position in computer programming.[7] [48]

157. The LaSalle course did not adequately teach students the basic principles on which computers work since it gave insufficient details on how a computer handles instructions, stores data, etc. A

[6] This impression was not dispelled by subsequent statements in connection with the title of Computer Programming trainee that the graduate would be capable of "making minor changes in existing programs." At best, the description of the course objectives was ambiguous on this point.

[7] This is the equivalent of an "entry level programmer" who in the definition of respondents' expert would be trained and ready to take on his first assignment without further formalized training (Safford 3560).

student who did not understand how the computer handles instructions would not understand basic computer programming (Hamblen 1187–88). LaSalle's computer programming course did not meet this objective.

158. The course, although it gave some examples of Coding in COBOL, did not give the student an opportunity to create his own code for his own problems, nor did the LaSalle student submit his coding for review by running it on a computer. The LaSalle course accordingly gave the student a superficial rather than a "working knowledge" of COBOL (Engel 992–93). The course objective of a working knowledge of COBOL was not met (Findings 148–49).

159. A graduate of the LaSalle basic computer programming course would not be able to code a flowchart into COBOL language, because of his inadequate experience in writing programs and in running them on the computer for feedback on errors (Hamblen 1208).

160. The LaSalle materials presented sufficient information to permit a student to read, understand, and perhaps modify a flowchart. However, a LaSalle student after having completed the materials would have difficulty creating a flowchart given a problem statement because he had no experience in analyzing and developing problems on his own and looking for alternative solutions (Engel 988).

161. LaSalle's course description presented flowcharts as an indispensable element of programming (Finding 148).[8]

162. Since LaSalle graduates would have difficulty in creating flowcharts, the course failed to adequately meet a major objective of the course teaching a student to "use flowchart information to write an actual computer program" (Findings 148–49, 160).

163. Nor, did the course fulfill its stated objective of teaching students to write actual programs for the latest model computers (CX 103F, 106F). The course was based exclusively on [49]the IBM 360 rather than the IBM 370 which had been introduced in 1970 as a replacement for the 360 (Engel 977; Hamblen 1203).

164. Graduates of the LaSalle basic computer programming course would not be able to change or modify existing computer programs, if computer logic were involved in such modification (Hamblen 1208). Accordingly, the course objective of learning to make minor changes in existing programs was not met.

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[8] In the computer programming industry, during the period 1973–1977, the more detailed type of flowcharting was replaced by structured COBOL which made detailed flowcharting unnecessary (Safford 3573). In that period, most companies were still using the type of flowcharting taught by LaSalle (Safford 3572).

165. The LaSalle materials did not require a student to run a program through a computer (Hamblen 1203).[9] Giving students an opportunity to run programs is an essential element in the learning process of a computer programming course (Hamblen 1202; Engel 977, 993).[10] Achievement of the course [50]objectives outlined by LaSalle was unlikely without access to a computer.

166. The typical LaSalle graduate with a high school education would not be able to enter the field as a computer programmer trainee[11] and perform functions such as conversion of flowcharts from rough to finished form and making minor changes in existing programs (Engel 1001–02).

Without further training, a graduate of LaSalle's computer programming course would be able to obtain various semi-clerical jobs, which would not be programming positions (Hamblen 1208–09, 1247–48).

167. The typical and ordinary LaSalle graduate would not be qualified to enter the computer field at the entry level as a computer programming trainee (Findings 157–66).[12] [51]

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[9] According to respondent's expert, it would be possible to learn programming "up to a point" without doing a compile (Safford 3591). He testified a desk check would enable a programmer to immediately find the majority of his errors through rechecking the manual and procedures (Safford 3594–95). Nevertheless, according to respondent's expert, a student might be unable to find an insubstantial error which would prevent a program from running (Safford 3604). A LaSalle graduate might desk check his program to the best of his ability and fail to discover errors which would prevent a program from compiling (Safford 3605). "You can't see a program debugged until it has been run through a computer" (Safford 3605). Moreover, respondent's expert considered it important for students in the training program under his supervision to run programs through a computer (Safford 3602).

In view of the foregoing testimony, more weight is given to the testimony of the Commission experts on the need for access to a computer for students of computer programming.

[10]

> You write a program on paper and then the next step, you have to convert that to machine-readable form somehow to get it into the computer. . .
>
> . . .[T]he computer is a deadly exacting device. Everything must be letter perfect and if you get the wrong character, you misspell a word or something like that. . .chances are it will reject the statement and print out some kind of error message which then you may have to go to a manual and look up. . .
>
> You really don't know how well you've done in writing a program until you have tried to run it on a computer. There's just no other way (Hamblen 1202; see Engel 977, 993).

[11] "The student does not acquire a job skill at the level to be considered for a position as a computer programmer trainee" (Report of the Accrediting Commission of the National Home Study Council dated January 31, 1976) (CX 330D).

[12] Respondent's expert, Herbert Safford, testified that his employer, GTE Data Services, Inc. (GTE), had a separate "start from scratch" training program and a more technical program for those who had "limited experience but training." Although he might be able to skip half the COBOL training, a LaSalle graduate would begin in the start from scratch program (Safford 3600–01). A LaSalle graduate in the case of GTE would be considered an entry level *trainee* rather than an entry level programmer (Safford 3601). In short, in the case of GTE, a LaSalle graduate would not have qualified as an entry level programmer which is the equivalent of a Computer Programming Trainee (See p. 47, n. 7).

The Commission's experts and respondents' experts had sharp differences in matters of underlying detail. Nevertheless, the ultimate conclusions on the qualifications of LaSalle's graduate as entry level programmers are not far apart.

168. Major elements of the course objectives set forth in LaSalle's Brochures were not[13] met (Findings 148–49, 157–66). Therefore, representations that the course would prepare graduates to meet the course objectives were misleading or deceptive.

169. Meeting the course objectives was prerequisite to LaSalle graduates qualifying as computer programming trainees which was the position respondents represented their graduates were trained to fill (Findings 150, 153–54).

170. The ordinary and typical graduate of LaSalle's computer programming course would not qualify as a computer programming trainee (Findings 157–69). Respondents' representation that the graduates of its computer programming course would qualify as computer programming trainees was accordingly deceptive.

171. Since LaSalle's basic computer programming graduates were not qualified for entry level jobs as computer programmer trainees, representations that there was a substantial demand for LaSalle computer programming graduates and that they could expect a substantial increase in income upon completion of the course (Findings 132–45) were false and misleading. [52]

C. Air Conditioning and Refrigeration

172. LaSalle represented that air conditioning and refrigeration was an opportunity field—a high paying rewarding career (CX 1, 4A, 5A; RX 20). By offering free booklets to start you on this rewarding career and through the representations made in its advertisements, brochures and by its sales representatives, LaSalle implied that a successful career in air conditioning and refrigeration could be achieved through study with LaSalle (CX 1, 2, 3; RX 20).

1. LaSalle Represented That There Was a Need or Demand for LaSalle Graduates in the Field of Air Conditioning and Refrigeration

173. In their advertisements, LaSalle stated that there was a big demand in the field even for newcomers.

Even the newcomer with the right training is going to be in demand. .and *well paid* (RX 20).

Service and installation men are needed. . . Newcomers are welcomed because of the fast growth of the field and short supply of trained men to handle all the work (CX 3).

[13] In view of this finding, further findings as to whether the course objectives in Respondents' Self-Evaluation Report submitted to the Accrediting Commission of the National Home Study Council (CX 3270) or the objectives in the "Curriculum Recommendations and Guidelines for the Community and Junior College Career Program in Computer Programming" (CX 815G) had been met would be superfluous.

AIR CONDITIONING & REFRIGERATION

Big demand for service and installation men in homes, commercial buildings, apartment houses, factories. Field welcomes trained beginners. Good pay, good future—with plenty of chances for a business of your own (CX 5A).

AIR CONDITIONING AND REFRIGERATION

Big futures in air conditioning—with plenty of chances to start a business of your own! Service and installation men are in urgent demand for homes, commercial buildings, apartment houses—[53]in food markets, industrial plants, ships and planes! Newcomers are welcomed because of the fast growth of the field and short supply of trained men to handle all the work. Send for the facts today (CX 4A).

174. When these general demand representations were read in conjunction with statements such as:

Why shouldn't you be one of the lucky ones? Right now, Wayne instruction will get you started toward a life time career (CX 2; RX 20).

For over sixty years LaSalle has been helping ambitious men start new and profitable careers (CX 3).

For a future in a growing service field that offers plenty of chances to start a business of your own someday—get into air conditioning and refrigeration. Wayne's free booklet tells you how (CX 1).

they created the impression that there was a need or demand for graduates of LaSalle's air conditioning and refrigeration course.

175. LaSalle's course brochures reinforced the demand impression created in the advertisements. The covers of CX 102 and CX 105 state:

America's becoming an air-conditioned nation (CX 102A, 105A).

176. The text of the brochures continue to inform the reader that there is a need or demand for air conditioning and refrigeration servicemen.

You're looking for a career in an industry that is growing, an industry that needs people.

ONE OF THE FAST-GROWING
INDUSTRIES IN AMERICA TODAY

I know of no other industry that offers a young man such a wide variety of opportunities. The alert young man who chooses the air conditioning and refrigeration industry as a career can look forward to a bright future in a prestige industry.

James B. Gray
E.I. du Pont de Nemours

The Air-Conditioning and Refrigeration Institute expects shipments of unitary air-

conditioning equipment (the type of equipment used in most home central-cooling systems) to rise from 2,434,000 in 1972 to an estimated 2,800,000 this year—an increase of 15 percent.

Air Conditioning and
Refrigeration Institute

(CX 102C)

According to the U.S. Government: "Continued fast growth of home air conditioning will contribute to very rapid employment increase for air conditioning mechanics."

U.S. Department of Labor,
Occupational Outlook Handbook

(CX 102E)

177. The brochures also represented that LaSalle training would enable you to enter this growing field. "Training will help you succeed in this important, growing field" (CX 102E). "Wayne will teach you the fundamentals of air conditioning and refrigeration" (CX 105E). The inference to be drawn from such representations was that there was a need or demand for LaSalle air conditioning and refrigeration graduates (see also Findings 175–76).

178. The inclusion of testimonials from successful LaSalle graduates not only showed that some LaSalle graduates were employed in the field but it added to the general impression that there was a demand for LaSalle graduates (CX 102D, 105L). [55]

179. As with LaSalle's other courses, sales representatives were instructed to repeat the employment claims made in the brochures (RX 102G, 128B).

2. LaSalle Represented That Its Air Conditioning and Refrigeration Graduates Would Increase Their Earnings

180. LaSalle made claims that air conditioning and refrigeration was a high paying career (CX 5A; RX 20). In some instances, air conditioning and refrigeration was coupled with other "opportunity fields" about which general representations of higher wages were made (CX 4A, 5A).

181. Reiterating the success through LaSalle theme, LaSalle represented that its correspondence course would prepare the individual to enter the field of air conditioning and refrigeration and command a high salary.

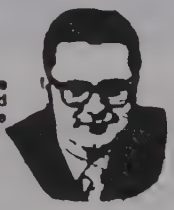
What does it take to earn higher pay? First, pick an uncrowded field where you have the chance to move ahead fast. Second, prepare with the right training—LaSalle training.

LaSalle has been helping ambitious men start new and profitable careers, for over sixty years. We can help you too (CX 4A).

This free booklet may start you on a high pay career in AIR CONDITIONING AND REFRIGERATION . . . For a future with higher earnings and plenty of chances to start a business of your own—get into air [56]conditioning and refrigeration (CX 2; RX 20).

183. In addition to making these statements about its ability to train people for higher paying jobs, LaSalle used testimonials to carry the success through LaSalle theme.

"After five years working for a chemical company . . . I was at a dead end, so I enrolled with LaSalle. Now I am out of my rut and my salary's up over $2,800 a year."
Charles B. Dunivan
Indianapolis, Indiana



"I am really grateful to LaSalle . . . In the past four years my income has increased over $9,000. I now have twenty people under my supervision."
Norbert Kaltan,
Ridgewood, New York

(CX 4A)

These testimonials appealed to the reader to take the LaSalle course and, like the individuals pictured and quoted, become a higher paid, successful individual. [57]

184. A combination ad, which included air conditioning and refrigeration, carried the following statements and testimonials.

WHO ELSE WANTS A BIG RAISE IN PAY?

Stuck in a rut? Tired of your dead-end job? Read how LaSalle spare-time training has helped others to move up to better paying positions with increased prestige.

Look at these pleased reports from LaSalle students. Many success stories of this kind come to us every year from people who began their career planning by mailing the LaSalle coupon for information.

LaSalle students have one ambition in common to get out of the ranks of the untrained and earn more money and respect in a better job. Isn't that your goal too?

Since enrolling with LaSalle my salary has doubled.

Robert Kubec
St. Cloud, Minnesota

In the past four years my income has jumped over $9,000.

Norbert Kaltan
Ridgewood, N.Y.

My salary has quadrupled since starting the course.

George R. Kelly
W. Bridgewater, Mass.

Thanks to LaSalle training. . .my salary has doubled.

Mrs. Mary M. Myberg
Los Angeles, Calif.

(CX 21) [58]

185. In presenting LaSalle's courses, including Air Conditioning and Refrigeration, to the prospective student, sales representatives fostered a dissatisfaction with present earnings and held out the promise of higher earnings after the LaSalle course (Finding 106; CX 153Y-DD).

3. LaSalle Represented That Its Graduates Would Be Qualified To Enter the Field of Air Conditioning and Refrigeration with No Further Training

186. In its advertisements, brochures and through its sales staff, LaSalle created the impression that its graduates would be completely qualified to enter the field of air conditioning and refrigeration. LaSalle represented that a graduate of the course would acquire the knowledge and skills necessary to perform the duties required of servicemen.[14] LaSalle's advertisements stated:

Build a future in air conditioning—with plenty of chances to start a business of your own. Learn how to service equipment for homes, commercial buildings, apartment houses—food markets, industrial plants (CX 16B). [59]

187. The following text about the air conditioning and refrigeration course was part of a combination ad with the headline—

Grow with the future. Train at home for one of these

6 TECHNICAL FIELDS

[14] It is disputed whether LaSalle represented it trained its graduates to enter the field as "mechanics" trained to diagnose and repair all problems found in air conditioning and refrigeration systems without supervision or whether LaSalle represented it trained students to enter the field as apprentices or trainees. Although the term "mechanic" was not included in text written by LaSalle in its course brochures, the term was used in testimonials and other quoted materials which were adopted by LaSalle for advertising purposes and should be considered as part of the representations made by LaSalle (CX 102E, N, 105L, N). In addition, LaSalle represented that its ordinary and typical graduate would be able to open his own business (CX 4A). Clearly, a LaSalle graduate operating his own business would not be viewed as an apprentice/trainee. Someone operating his own business would not receive further training or supervision.

Build a future in air conditioning—with plenty of chances to start a business of your own! . . . Newcomers are welcomed because of the fast growth of the field and short supply of trained men to handle all the work (CX 3).

188. Taken as a whole, CX 3 encourages the reader to train with LaSalle, enter the field of air conditioning and even start his own business based on his LaSalle training.

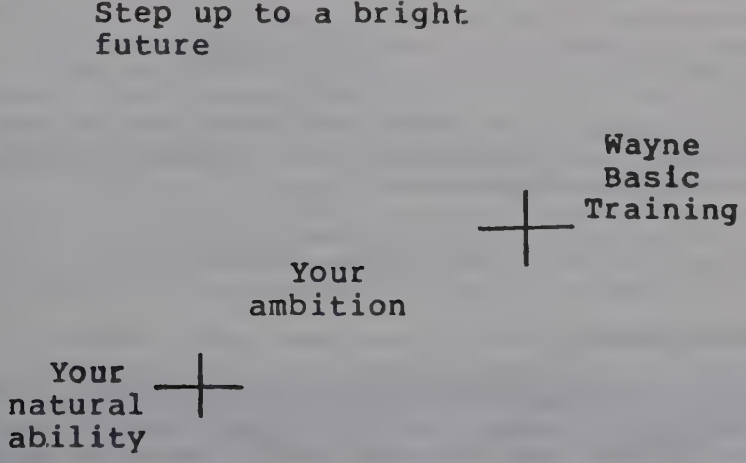
189. Some advertisements, such as CX 1, did qualify statements about the ability of LaSalle graduates to be employed in the field with words like "start a business of your own *someday*" and "Trained people can look forward to a rewarding career *once they gain on-the-job experience*" (emphasis added). However, the overall impression conveyed by respondents' advertisements was that the LaSalle air conditioning and refrigeration graduate would be qualified to enter the field and service equipment without further training or experience.

190. In its course brochures, LaSalle continued the theme that success in the field of air conditioning and refrigeration was attainable through LaSalle.

TRAINING WILL HELP YOU
SUCCEED IN THIS IMPORTANT,
GROWING FIELD

In this world, nothing comes just by wishing for it, and the opportunities in the refrigeration and air conditioning industry are no exception. You have to want them badly enough to work for them. [60]

Training is the very best way for you to start. The solid kind of training you can receive from Wayne School—if you qualify (CX 102E).



(CX 105D)

191. The following statement prefaced the outline of the course in air conditioning and refrigeration:

This 37-lesson course has been especially designed to prepare you to enter the growing field of air conditioning and refrigeration and to give you the *basic technical knowledge that will help you move up faster on the job.* It is a practical course which will teach you the actual procedures used in servicing the most widely used kinds of cooling equipment (CX 102J).

The outline concluded with:

YOU NOW UNDERSTAND THE PROCEDURE INVOLVED IN SERVICING AIR CONDITIONING AND REFRIGERATION SYSTEMS. YOU ARE READY TO START OUT IN THE FIELD (CX 102M). [61]

192. The closing statement unequivocally represented that the LaSalle graduate would be ready to service air conditioning and refrigeration equipment.

193. Respondent's course brochures also contained testimonials from successful graduates (CX 102D, 105L). These testimonials gave the impression that LaSalle graduates were employed in the field as a result of their LaSalle training.

My training has helped me get a job with a Frigidaire dealer in my town. Now I repair refrigerators and freezers, with chances for advancement.

John A. Kemp
Truth or Consequences, New Mexico
2/27/74

The Wayne course gave me enough insight into air conditioning to start my own sales and service business.

James D. Hanger
Baraboo, Wisconsin
1/5/75

The course has opened doors to a brand new life and I love it. When I was only halfway through the course, I was hired as a serviceman and mechanic. Now they depend on me for most of their refrigeration work.

Vincent Palmer
Bronx, New York
3/3/74

(CX 102D, 105L)

The fact that some graduates in their endorsements stated that they started their own business made the promises of LaSalle's advertisements come alive. Such testimonials tended to confirm the representation that the LaSalle graduates were qualified to enter the field of

air conditioning and refrigeration as servicemen without further training or experience. [62]

4. Expert Opinion as to LaSalle's Training and the Employability of LaSalle Air Conditioning and Refrigeration Graduates

194. LaSalle represented that its air conditioning and refrigeration graduates would be qualified to enter the field as servicemen without further training or experience (Findings 186–93). Although the advertisements and brochures referred to "entering" the field or of "starting" a career in air conditioning and refrigeration, the overall representation referred to the skills level of a mechanic rather than that of an entry level position as an apprentice or trainee (CX 1, 2, 3, 102, 105). In addition, references to starting one's own business reinforced the impression that success as an air conditioning and refrigeration serviceman was to be expected with LaSalle alone.

195. A mechanic or serviceman is an individual who has the expertise, training and knowledge to make all necessary repairs without supervision (Laham 733; Lupson 3999). Hands-on experience is a necessary prerequisite to becoming a qualified serviceman (Ritchie 1084; Wintersdorf 1525–26, 1581–82; Lupson 3999, 4089–90, 4096). It is apparent that a correspondence course with no laboratory experience cannot provide the hands on training necessary to become a serviceman. In proposed Finding 45, respondents agree with the experts that LaSalle's course did not prepare the ordinary and typical graduate for employment as a serviceman. Respondents state:

> 45. The Basic Air Conditioning and Refrigeration Service Course is designed to provide knowledge of the fundamental principles of air conditioning and refrigeration and to provide basic instruction in the service and repair of most types of air conditioning and refrigeration equipment, in order to prepare a student with some mechanical aptitude or interest for entry-level employment opportunities in the field (CX 102N, 105N). The course is not intended to qualify students, with no additional training or experience, to diagnose and repair all problems found in air conditioning and refrigeration systems without supervision, *i.e.*, to be a "mechanic" as that term is defined by some, but not all, those familiar with the industry (see Laham 733; Wintersdorf 1525; Lupson 3999; *but cf.* [63]McCarty 594, defining an "entry-level service mechanic" as a "rookie" with "very little experience in the field").

196. LaSalle's course does indeed provide knowledge of the fundamental principles of air conditioning and refrigeration (Laham 732; Wintersdorf 1522, 1525; Lupson 3998–99); however, the training was not sufficient to qualify the graduate for employment as a mechanic.

197. While some LaSalle graduates may have found employment as servicemen, the ordinary and typical LaSalle graduate was not qualified to be employed as a serviceman without further training or supervision. Nor, would the ordinary and typical graduate be able to open his own business in air conditioning and refrigeration service and repair since such an operation would require the skills of a mechanic with hands-on experience (Findings 195–96). To the extent that LaSalle represented in its advertisements, brochures and through its sales representatives that the ordinary and typical LaSalle air conditioning and refrigeration would be qualified to enter the field as a serviceman, such representations were false and misleading.

198. LaSalle also represented that there was a demand for LaSalle graduates (Findings 173–79). The demand representation made by LaSalle was in connection with an increased demand for air conditioning and refrigeration servicemen (CX 102). LaSalle graduates were not qualified to be servicemen (Finding 196).

199. Therefore, the demand and earnings representations made in conjunction with the representation that LaSalle graduates would be qualified for employment as air conditioning and refrigeration servicemen were false and misleading.

V. Course Structure And Refund Policy

A. Front End Loading

1. Course Structure

200. Respondents' correspondence course materials consisted of volumes of textual material, examinations which were submitted to the school for evaluation and return, self-test exercises which were evaluated by the students at home and, for some courses, additional technical materials (RX 151; Marshall 1969). In LaSalle's correspondence courses, [64]the amount of reading for each submitted examination increased as the course progressed (Marshall 1973–74). In many of respondent's courses, including computer programming and interior decorating, there were more chapters of text than examinations. This was consistent with the practice in a number of other correspondence schools and was considered by some to be educationally beneficial (Marshall 1969, 1984–86).

The result of this course structure was that LaSalle students were often required to submit examinations more frequently at the beginning of the course than at the end (RA 45–48; Marshall 1973–74).

201. The term "front-end loading" has been applied to LaSalle's course structure, a structure which places most of the lesson assignments to be submitted at the beginning of the course. When used in this decision front-end loading shall be defined solely as the uneven distribution within LaSalle's course materials of lesson assignments to be submitted.

202. LaSalle did not send its students an entire set of course materials at one time. Rather, LaSalle mailed the course materials in segments with the submission of a key examination triggering the next shipment (CX 151UU, XX; RX 101F, 102F, 103F, 133F).

203. In some courses, LaSalle did include course outlines with the first shipment of course materials. The outlines described at what points in the course lesson assignments were required to be submitted (RX 151S, 153–61). LaSalle did not have a uniform policy about furnishing outlines, but left it to the judgment of the course supervisor to make the decision for each course based on pedagogical reasons (Marshall 1971–72).

2. LaSalle's Quartile Tuition Policy

204. LaSalle's course structure was related to its tuition refund policy. Since 1973, all refund policies applied have been based on a fraction—the number of lesson assignments submitted by the student over the total number of lesson assignments in the course (CX 425BB).

205. The most widely applied refund policy was that of the National Home Study Council (hereinafter cited as NHSC). Under that policy, a student owed a registration fee plus 25 percent of the total tuition obligation if he submitted less than 25 percent of the lesson assignments to LaSalle for review; 50 percent of the tuition was owed if the student [65]submitted more than 25 percent but less than 50 percent of the lesson assignments and the total tuition was owed when the student submitted more than 50 percent of the lesson assignments (CX 200–01; RX 856 (Federal Contract)).

206. Various state laws and regulations, changing from time to time, required different refund policies for students residing in those states. In those states, LaSalle applied the state policy and incorporated it in the enrollment contract form (CX 217, 225, 238, 248, 261, 271, 273). The "Federal" form of the enrollment contract was the most widely used form (Martins 2668).

207. As of 1978, respondents modified their quartile tuition policy. According to LaSalle's most recent contracts, students were obligated to pay, in addition to a registration fee, 10 percent of their tuition if they submitted less than 10 percent of their lesson

assignments, 25 percent of their tuition if they submitted more than 10 percent but less than 25 percent of their lesson assignments, 50 percent of their tuition if they submitted more than 25 percent but less than 50 percent of their lesson assignments, and 100 percent of their tuition if they submitted more than 50 percent of their lesson assignments (CX 199 (Federal Contract)).

208. The refund policy applicable to a particular student was governed by his enrollment contract. The refund policy on that contract depended on the date of enrollment and the student's state of residence at the time of enrollment (Findings 204–07).

209. LaSalle's enrollment contracts generally stated the applicable refund policy in terms of percentages of "assignments completed" between 1973 and 1975. Beginning in 1976, LaSalle revised this language to percentage of "lesson assignments submitted" to LaSalle (Before 1976 CX 201; after 1976 CX 199, 200, 202; RX 856). The contracts did not state that the readings between "lesson assignments" increased as the course progressed, nor did other materials furnished to students before enrollment (CX 176–275; RX 851–52, 856). Prior to 1979, LaSalle's contracts did not state the total number of lesson assignments to be submitted in a given course, except where required by state law (CX 199, 200, 201, 202; RX 856). The total number of lessons was listed in the course brochure; however, the cancellation and refund policy was not stated in the brochure (CX 101N, 102J, 103F, 104N, 105H, 106F).

210. Since a student's tuition obligation was derived from a percentage based on the number of lesson assignments submitted, the total number of lesson assignments to be submitted in a given course was a material fact which the student needed to know in order to be able to calculate his tuition obligation. [66]

3. LaSalle's Knowledge of Student Confusion concerning the Refund Policy

211. Respondents were placed on notice by students, attorneys general, consumer organizations, and others that students were confused as a result of LaSalle's failure to disclose the existence of front-end loading and its interaction with the quartile tuition policy (see for example; Mastrangelo 758–74, 780–84; Mseitif 1609–17; Moore 1638–46; Deet 1689–1709; CX 720–30, 787–88).

212. LaSalle's officials were aware of the confusion among students regarding the interaction between front-end loading and LaSalle's quartile tuition policy (Israel 1979–80; CX 327LLLLLL). In the Self-Evaluation Report submitted to the NHSC, LaSalle stated:

8. Proper balance of the examination schedule: . . .we have come to realize that many of our courses require revision in the pattern of examination submissions. . . .we have followed the classic tenet of the home study field, which generally calls for more frequent submissions during the early portions of home study courses, with less frequent submissions required after the student is off to a sound start.

However, this type of structure can create a problem under a refund policy based on the number of assignments or lessons submitted. In 1974 it became apparent that in many of our courses the difference in the scope of materials covered by submissions in the early and later portions of several courses had created just such problems. In January 1975, therefore, we began revisions of the submission patterns in several courses. Courses affecting a majority of our students already have been revised. The remainder of the courses in which such problems exist will be amended in the near future. We intend to continue with revisions of the remaining courses in which such problems exist. [67]

213. Although LaSalle did make some changes in the examination distribution scheme of its courses, at least two courses (interior decorating and computer programming) continued to be front-end loaded after August 1975 (RA 45–48).

B. Terminology Confusion

1. Respondents Failed To Uniformly Define Contract Terms

214. Respondents' course materials consisted of reading materials, self-tests, lesson assignments to be submitted to LaSalle, and, for some courses, additional technical materials (Finding 200).

215. The course materials and course brochures used several different terms for lesson assignments to be submitted to LaSalle. These lesson assignments, on the basis of which the student's tuition obligation was calculated, were called: "lessons," "assignments," "projects," "examinations," "submissions" and "lesson assignments" (CX 106H, I, R, 115J, 119Q; Hetzel 3121–22).

216. In some instances, different terms were used in the same brochures to describe lesson assignments to be submitted to LaSalle:

2. LaSalle is as near as the closest mailbox. You simply drop each completed *lesson* into the mail. You set your own hours for the completion of each *assignment.*

3. Your *assignment* arrives at LaSalle. It is immediately forwarded to a faculty specialist in your area of training (CX 101I, 104I, 106H) (emphasis added).

1. You receive your student materials and *lesson assignments* a group at a time, so you can work at your own speed. [68]

2. When you have studied a *lesson,* you do the *assignment* and send it to Wayne.

3. An instructor goes over your *exam,* checks the answers, adds helpful comments, and mails it back to you (CX 102G) (emphasis added).

217. Not only were a number of terms used interchangeably to describe the lesson assignments to be submitted to LaSalle, but the term "lesson" was also used to describe both the textual reading material and the lesson assignments to be submitted (CX 101I, 104I, 106H; RX 151F).

218. LaSalle's progress charts, which were included with some courses, used the terms "exams" or "examinations" to refer to lesson assignments submitted to LaSalle (RX 151, 153-61).

219. Prior to May 1976, a student's tuition obligation, pursuant to LaSalle's contract, was based on the number of "assignments completed" (Finding 209; CX 201, 204, 207, 210, 213, 216, 218, 221, 228-29, 232-33, 236, 239-40, 243, 245-46, 250, 252, 255-57, 260, 262-63, 269). Thereafter, a student's contractual obligation was defined in terms of "lesson assignments submitted" (Finding 209; CX 199-200, 202-03, 205-06, 208-09, 211-12, 214-15, 219-20, 222, 226-27, 230-31, 235, 241-42, 251, 253-54, 258-59, 266-68; RX 851, 856).

220. Prior to February 1979 (RX 852D), respondents' contracts did not define either "assignments" or "lesson assignments", the operative language used in the contracts to calculate a student's tuition obligation. In addition, LaSalle did not define the contract terms in the course materials nor did LaSalle consistently use the same term in its materials for lesson assignments submitted (Findings 215-18; CX 276-78, 932-34).

221. The inconsistent use of terms to define and distinguish respondent's course materials, which consisted of reading materials, self-tests, lesson assignments to be submitted to LaSalle and, for some courses, technical materials, resulted in confusion as to the meaning of the contract terms "lesson assignments submitted" and "lessons completed." Because students did not know what constituted "lessons completed" or "lesson assignments submitted", they were unable to calculate their tuition obligation. [69]

2. LaSalle's Knowledge of Student Confusion regarding Terminology

222. Respondents had notice from students, attorneys general, consumer organizations, and others that students were confused and deceived by the use of different terminology in the course materials, brochures and contracts (see, for example, CX 731-37, 751-52, 769-76).

223. Although in 1976 LaSalle did change the terminology used in the refund clause of its contracts from "lessons completed" to "lesson assignments submitted", it did not make the language used in its course materials, brochures, progress charts, and contracts

uniform (Findings 209, 215–19). Because different terms were used to refer to lesson assignments submitted to LaSalle, the confusion continued and students were unable to calculate their tuition obligations.

C. Respondents Failed To Disclose Material Facts respecting Students' Tuition Obligations

224. Respondents did not disclose all of the information needed to calculate the tuition obligation at the time of cancellation (Findings 210, 221). Information about the nature and extent of a student's tuition obligation and about the ability to cancel his contract with LaSalle and receive a refund was material to a student's decision to enroll and to his decision to terminate enrollment.

225. The cancellation and refund policy was separately set out in the contract. Representatives were instructed to read the cancellation and refund policy clause to prospective students prior to their executing the contract (CX 153XX; RX 131A–C). In addition, prospective students were admonished in the contract itself not to sign the contract before reading it (for example, CX 200–02). Such actions on the part of LaSalle, apart from any actions or concerns personal to the prospective student, imbued the contract's cancellation and refund clause with an importance that would make it a material part of any decision to enroll.

226. LaSalle's failure to disclose the number of lesson assignments in the contract and to use a uniform term for "lesson assignments to be submitted to LaSalle" were also material, after commencement of the course, to a student's decision to terminate his studies with LaSalle. No matter what reason a student had for terminating his enrollment with LaSalle, the cancellation policy had the capacity and the tendency to affect the timing of that decision. [70]

For example: once a student submitted 50 percent of the lesson assignments, early termination due to lack of funds would be futile since the student would already be obligated for the total tuition. Obviously, the percentage of lesson assignments he had submitted would be a material fact in his decision to terminate.

227. Both the number of lessons in a particular course and the meaning of the contract terms "lessons completed" and "lesson assignments submitted" were material facts in calculating a students' tuition obligation which were not disclosed. The non-disclosure of these facts had the tendency and capacity to deceive students as to the extent of their tuition obligation.

228. It is a violation of Section 5 of the Federal Trade Commission Act for a seller not to disclose a material fact.

VI. The Selectivity Allegations

A. LaSalle's Enrollment Standards and Policy

229. Sales representatives were instructed that:

The qualified student is one who has the mental ability, the desire for improvement, the necessary time and desire to study and the ability to meet tuition payments (CX 151T).

230. The following educational prerequisites for enrollment in LaSalle's courses were in force:

The basic educational requirement observed by LaSalle is that a prospective student has had sufficient education to enable him or her to benefit from the course of instruction. No applicant can be enrolled unless, at a minimum, he or she is able to:

1. Read standard 9–10th grade English; [71]

2. Follow instructions as to lesson submission procedures.

All of our courses are in English only. Someone who does not speak English well would probably have difficulty reading and comprehending the material, and should not be recommended for enrollment.

For specific courses there are additional minimum educational requirements as indicated below. The Life experience of certain mature applicants may be accepted in lieu of formal education requirements. Such exceptions must be individually approved by the Director of Education (CX 151T–U; see also CX 327WWWW).

231. The minimum educational level for the Air Conditioning, Computer Programming, and Interior Decorating courses was four years of high school. However, in the case of the Air Conditioning and Interior Decorating courses, students over 21 could be enrolled if they had two years of high school (CX 151U).

232. LaSalle required no prior employment or experience in the field of training for which a prospective student applied (CX 327XXXX).

233. LaSalle sales representatives rejected students because they could not meet respondents' minimum education requirements, inability to read English, and physical handicaps (Werner 2799–2802; Martins 2643–44; Terrana 3860–62).

234. For at least one sales representative the prime consideration in determining whether to recommend enrollment was whether the prospective student could afford the tuition (Shulock 379).

235. In 1975, LaSalle conducted a lead control program from the

latter part of March to the latter part of August for the purpose of determining why prospective students did not enroll or why no sale was made (Pierce 2968–69, 2985; RX 227A–H). The lead control form contained nine reasons for no enrollment or no sale[15] including "not interested," "under age," "not [72]qualified", etc. (RX 224A–B, 227B). "Not qualified" meant persons who did not meet the educational requirements established by LaSalle, persons with inadequate ability to read English, and in a few cases, the physically handicapped (Pierce 2982–83). During the course of the lead control program, representatives were required to retain every lead for a prospective student whom they did not enroll. They were to check on the lead form the reason the prospective student was not enrolled (RX 227B, H). The lead control program accounted for approximately 58 percent of the leads issued in that period (n. 16).

236. A tabulation covering the national totals for the last 12 weeks of lead issuance in the lead control program showed that of the total number of sales made the percentage of those "not qualified" was 68 percent. Of the total number of leads issued 2.7 percent were rejected as not qualified (Chakmakjian 3804–18; RX 226).[16]

237. After contracts were received by LaSalle's Home Office from the field, they were reviewed for educational requirements by the Enrollment Department and in a questionable case, the contracts were referred to the Education Department (Hetzel 3093; Marshall 1910–11, 1917–18).

B. Representations That LaSalle Screened Students

1. Representations That Prospective Students Had To Qualify To Be Admitted or Accepted by LaSalle

238. The cover letter sent by LaSalle to prospective students stated:

He [the local LaSalle representative] *will talk to you about your* needs and [73] *qualifications for training,* and give you any further information you may require. He does this as part of his job, and there is no obligation of any kind (CX 151X) (emphasis added).

[15] A "no sale" was a lead called on but not sold (RX 227D).

[16] Total number of leads issued for the 12-week period was 127,652; 5,077 leads were converted into sales; and 3,439 leads were rejected as not qualified (RX 226A–B).

Not all leads issued in the period were accounted for by the lead control program or the tabulation. The dispositions received tabulated in RX 226 accounted for 57.9 percent of the leads issued (Chakmakjian 3810; RX 226A).

239. Respondents' course brochures repeated the theme that prospective students had to qualify for admission, *e.g.:*

The LaSalle Admissions Policy

LaSalle is open to all qualified students. In accepting applicants for admission, a primary concern is their willingness to do the work involved. This means a minimum of five or six hours a week devoted to study (CX 103M, 106M; Computer Programming Brochures) (emphasis added).

* * * * * * *

Wayne School is open to all *qualified students.* In *accepting applicants* for *admission,* a primary concern is their willingness to do the work involved. . .

If you *apply* for *admission* to Wayne, you will be asked to state the sincerity of your purpose (CX 102 O, 105 O) (emphasis added).

* * * * * * *

IF YOU ARE ACCEPTED, WE WILL TRAIN YOU IN THE FUNDAMENTALS OF AIR CONDITIONING/REFRIGERATION SERVICE (CX 102F, 105E) (emphasis added).

Training is the very best way for you to start. The solid kind of training you can receive from Wayne School—*if you qualify* (CX 102E; see also CX 105D) (emphasis added).

If your answer to any of these questions is "yes," and *if you think you are qualified* I personally urge you *to apply for admission* now (CX 102P) (emphasis added). [74]

240. Sales representatives during their training for the standard sales presentation were instructed that:

The heart and core of this procedure is the qualifying interview. *This technique requires the prospect to tell you why he's qualified* for the course he's inquired about (CX 153D) (emphasis added).

* * * * * * *

. . . [The prospective student] has to convince himself and you that he qualifies. . . . (CX 153I).

they were further instructed to create the impression that:

the prospect. . .has to qualify for entry into LaSalle. Acceptance is not automatic (CX 153L).

. . .with the term qualification questionnaire, we've reemphasized the fact that he must qualify—acceptance is not automatic. . . . (CX 153P).

acceptance is not automatic. That he must show that he qualifies and that this will depend on the outcome of your questioning. . . . (CX 153P, Q).

. . .the fact that he must measure up to LaSalle's requirements, that he must convince you of his merits. . . . (CX 153Q).

241. In line with the foregoing instructions, LaSalle sales representatives were instructed to say the following to prospective enrollees when met with objections at the door:

I'm here to help you find out if you have what it takes to qualify. . . . (CX 155I).

We want only high quality students. I can see if you qualify then recommend [75]your acceptance. May I step in? (CX 155I; see also CX 167G–H).

242. Respondents represented that prospective students must qualify for admission. Moreover, the Standard Sales Presentation which LaSalle sales representatives were trained to use had the tendency and capacity to create the impression that the burden was on the prospective student to show that he was qualified (Findings 240–41).

243. The use of the "Confidential Qualification Questionnaire" (CX 154H) during the "intensive qualification" portion of the sales presentation (CX 154D) had the capacity and tendency to reinforce the impression that prospective students had to qualify for admission to respondents' courses.

2. Representations That Certain Aptitudes Were Helpful or Required in the Case of Particular Courses

244. In their advertisements for the interior decorating course and in their interior decorating course brochures, respondents made the following statements:

You'll be able to put your natural talents and creative urge to use in designing beautiful and exciting rooms for clients (CX 6A; Advertisement).

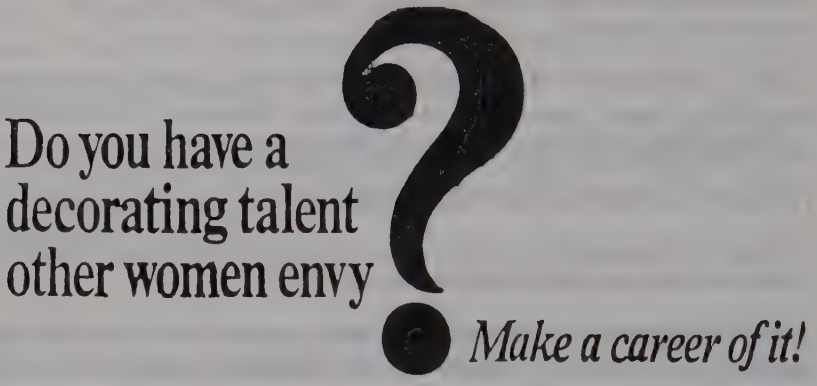
You may be one of those with natural talent for this fascinating field—a talent that could be developed through LaSalle instruction (CX 6B).

. . .Step by step, you are shown how to make the most of your creative ability. . . . (CX 7B, 30B).

You'll be able to put your natural talents and creative urge to use in designing beautiful and exciting rooms for clients (CX 8A).

Even if you've done no decorating, you may be one of many women with unsuspected talent in this direction—talent just waiting to be discovered (CX 9A). [76]

Decorators can put their natural talents and creative urge to use in designing beautiful and exciting rooms for clients (CX 30A, 31).



(CX 32)

Interior Decorating

A fascinating field where you can put your creative talents to practical use. . . . (CX 45).

But even if you've done no decorating and have no business experience, you may be one of many people with talent in this direction—talent waiting to be discovered (CX 101C).

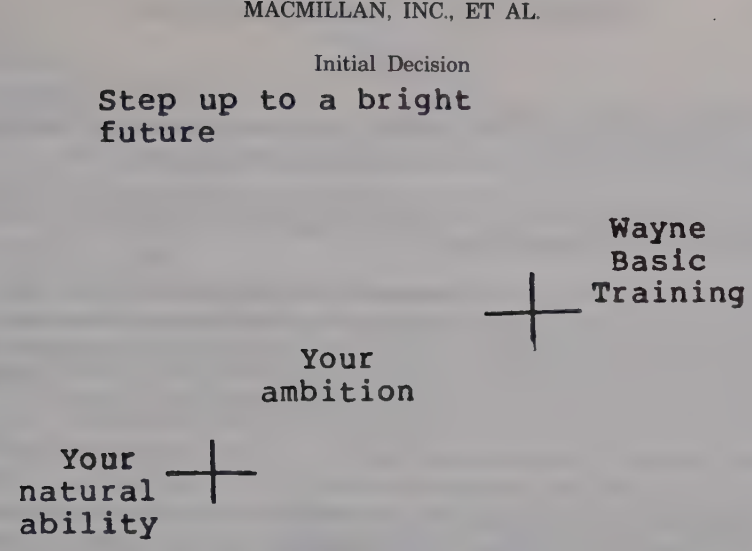
245. The foregoing representations had the capacity and tendency to create the impression that a talent for decorating was prerequisite to or helpful in benefitting from or successfully assimilating the Interior Decorating course materials.

246. In their advertisements for the basic computer programming course, respondents advertised that: [77]

. . .All that it takes to start training is a high school education and a logical mind no technical background required. . . . (CX 3, 4A, 5A, 12C, 16C).

247. Such representations had the capacity and tendency to create the impression that a logical mind was a necessary aptitude to benefit from or to successfully assimilate the course materials.

248. Respondents, in the Air Conditioning and Refrigeration course brochures, stated:



(CX 105D)

Certain courses have special requirements. To enroll in the Wayne course *in Basic Air Conditioning and Refrigeration, you should have mechanical aptitude* and at least two years of high school (CX 102 O, '74 Brochure) (emphasis added).

Education Requirements: To enroll in this program, you must have completed two years of high school if over 21 years of age, and four years of high school if under 21 years. *A mechanical aptitude is also helpful* (CX 105 O, '76 Brochure) (emphasis added).

249. The foregoing representations had the capacity and tendency to create the impression that mechanical aptitude, [78]interests or ability were prerequisite to or helpful in benefitting from or in successfully assimilating the Air Conditioning and Refrigeration course materials.

250. The courses were written with characteristics such as a logical or mechanical aptitude in mind (Marshall 1906).[17] [79]

---

[17] Q. And it's possible to test mathematical aptitude in certain instances, isn't it?
A. Yes.
Q. How does one test a prospective students ability to use their hands?
A. Manual dexterity.
Q. How do you test for that?
A. That, I do not know.
Q. The ability—the prospective student having a logical mind is one of the standards that has been set for the computer programming course, is it not?
A. That's not only the enrollment standard, no.
Q. The brochures indicate that you should have, however?
A. Yes, that helps.
Q. Does LaSalle test for that, do you know?
A. No, sir.
Q. Does LaSalle test manual dexterity?
A. No, sir.
Q. Would you say that the courses are written with those backgrounds in mind?
A. Yes, sir (Marshall 1906).

3. Representations That LaSalle Screened Prospective Students To Ensure That They Would Benefit From The Course

251. Salesmen were instructed to say, as part of the pre-screening talk in the Sales Presentation:

. . .*I want to be sure that we have a program that is right for you, Mr. Miller, and that you are right for the program.* As a leading correspondence school, *LaSalle will only accept students who can benefit from its program* of study. *To determine whether you can benefit* Mr. Miller, we'll be discussing your reasons for wanting more education and your desire and ability to study and succeed (CX 168D) (emphasis added).

* * * * * * *

. . .*I must be sure that we have a program that is right for you,* Mr. Miller *and that you are right for the program.* After all, no school wants to accept unqualified applicants. . . . (CX 153I) (emphasis added).

252. The theme that prospective students were screened to select those who would benefit from a particular course was continued in respondents' Retail Installment Contracts.

Carefully screens students for admission and has demonstrated ample student success and satisfaction (CX 199D, 200D, 202D).

* * * * * * *

LASALLE WANTS TO ENROLL ANY PERSON WHO:

1) HAS ENOUGH FACTS FROM SCHOOL BROCHURES TO FEEL HE OR SHE CAN BENEFIT FROM ANY PARTICULAR COURSE (CX 199E, 200E, 202E). [80]

253. Representations that LaSalle's salesmen wanted to be sure that a course was "right" for a prospective student or that it was respondents' policy to enroll those prospective students who would "benefit" from a course had the capacity and tendency to create the impression that respondents' screened prospective students prior to enrollment for the specific aptitudes requisite or helpful to particular courses over and above the standard age and educational requirements applicable to LaSalle's courses generally. Furthermore, such representations had the tendency and capacity to create the impression that LaSalle accepted only those students who could benefit from particular courses and assimilate their contents.

254. The impression that respondents screened prospective students prior to enrollment for the aptitudes helpful or necessary to benefit from and assimilate specific course materials (Findings 238–43, 251–53) was reinforced by other representations that specific aptitudes such as talent for decorating, a logical mind and mechani-

cal ability were required for or helpful in the case of particular courses (Findings 244–49).

255. In fact, LaSalle, because of its open enrollment policy, instructed its instructors to report students who *after commencing the course* appeared unable to benefit from such instruction (CX 327XXXX).[18] [81]

256. LaSalle did not in fact screen prospective students with respect to the specific aptitudes necessary or helpful to assimilating or benefitting from the particular course (Marshall 1906; RA 49, 51, 53, 59).

257. The combined effect of respondents' representations that prospective students had to qualify for admission (Findings 238–43), that it was LaSalle's policy to enroll prospective students who could "benefit" from or were "right" for particular courses (Findings 251–53), and that certain aptitudes were helpful in certain courses (Findings 244–49), had the tendency to create the impression that over and above the standard minimum age and educational requirements generally applicable, respondents were selective in enrolling those students who had been screened to determine that they would benefit from particular courses.

258. Such representations were false, misleading or deceptive since respondents did not screen prospective students for specific aptitudes helpful to successful completion or assimilation of specific courses.

VII. The Vocational Value of LaSalle's Correspondence Courses

A. The Commission Survey To Measure Success of Vocationally Motivated Graduates of LaSalle Correspondence Courses

1. The RPC Survey

259. Resource Planning Corporation (hereinafter cited as RPC), at the request of the Federal Trade Commission, conducted a survey to evaluate the experience of persons enrolled in three LaSalle Extension University courses, computer programming, interior decorating, and basic air conditioning and refrigeration. Two primary areas were to be investigated: first, what motivated the students to take their course and how, if at all, LaSalle or its

[18] [*Because LaSalle has*] *an enrollment philosophy somewhat akin to today's open enrollment policy* of many American colleges and universities, *LaSalle. . . .tries to monitor early lessons carefully.*[LaSalle's] *instructors are asked to report students who appear unable to benefit from the course instruction.* In this way, such students may be advised of the need to improve. If no improvement occurs, the student is terminated and his contract obligations rescinded (Self-Evaluation Report submitted by LaSalle to Accrediting Commission of NHSC August 7, 1975; CX 327XXXX) (emphasis added).

representatives influenced that motivation, and second, what was the vocational and financial experience of the individuals taking such courses (CX 279C).

260. Prior to conducting the survey of former LaSalle students, RPC had conducted similar surveys of other correspondence schools for the Federal Trade Commission (Chambers 156; RX 271RR). RPC drew on its experience in [82]conducting the prior surveys when it conducted the LaSalle survey (Chambers 160).

261. RPC, when it drafted survey instruments for another correspondence school survey for the FTC, used the most recent survey instrument as a model and drafted the new instrument by modifying the one used in the preceding survey (Chambers 206–07). RPC interviewed no LaSalle student or graduate before drawing up the questionnaire used in the RPC survey of LaSalle (Chambers 207–08).[19] The model for the LaSalle survey instrument was the questionnaire used in the International Correspondence Schools survey (Chambers 206–07, 211).

262. The RPC survey was conducted sometime after September 1976 (RX 264B).

263. RPC's analysis was limited to vocationally motivated students and findings herein are limited to that part of the RPC survey relating to vocationally motivated graduates of its courses.

264. The graduate group represented all graduates of LaSalle between the period January 1974 and December 1975 (CX 279D).

265. The RPC survey instrument with a cover letter was mailed to the sample groups. Two weeks later a second mailing went to those who did not respond to the first mailing. After the two mailings, RPC conducted a telephone survey in order to complete the survey (CX 279D). [83]

266. After completion of the data gathering portion of the survey, the final sample and response rate of the RPC survey were as follows:

Courses	*Final Sample*	*Response Rate*
Computer Programming Graduates	276	57%
Interior Decorating Graduates	260	62%
Basic Air Conditioning and Refrigeration Graduates	273	61%
Computer Programming Nongraduates	296	27%
Interior Decorating Nongraduates	298	28%
Basic Air Conditioning and Refrigeration Nongraduates	296	31%

[19] The best way to develop questions and precoded answers to a survey is to interview a panel of individuals from the pool of survey respondents (Linden 4177–79). However, it was RPC's judgment, because of experience with the preceding surveys in several of which pilot tests were done, that there was no need for such a procedure (Chambers 208).

Of the nonrespondents, the vast majority had moved, leaving no forwarding address.

(CX 279E)

267. RPC attempted to determine whether a discernible difference existed between respondents and nonrespondents to its survey; it selected region of residence for this comparison. No statistically significant differences were found after performance of a Chi-square test.[20] On that basis, RPC assumed that there was no reason to believe that the nonrespondents would have responded differently, had they replied to the survey (CX 279E–F; Chambers 178–79). However, the Chi-square test on the basis of region would not disprove bias in the form of self-selection resulting from a grievance against LaSalle if this factor were present in all regions (Zeisel 2605–06). A bias founded on grievance is psychological and there is no real way to measure it (Linden 4209–10).

268. RPC defined a vocationally successful individual as one who obtained a job *or* salary he expected and who could not have obtained *either* without taking the LaSalle course (CX 279F).

269. RPC defined a vocationally unsuccessful individual as one who sought employment but who was unable to obtain any job in the field of his correspondence course since graduation (CX 279F). [84]

270. The RPC survey found that the breakdown of those taking the course for vocational reasons was as follows:

	Total	*Comp.*	*Dec.*	*Air*
Number	258	94	74	90
Percent	53%	59%	46%	54%

(CX 279G)

271. Two-thirds of the respondents to the RPC survey indicated that LaSalle, either through its advertising materials or its representatives, led them to believe that new or better jobs would be available in the field of their correspondence course and that completion of the course would fully qualify them for new or better jobs in the field (CX 279H).

272. Broken down by course, the RPC survey found that LaSalle through its advertising or representatives had led LaSalle graduates to the following beliefs in the percentages indicated:

[20] The Chi-square test is a test which tests the likelihood that one distribution differs from another distribution as a matter of chance or because of a real difference in the populations involved (Zeisel 2589–90).

a) New or better jobs would be available to the graduate in the field of his correspondence course upon completion of the course for which he enrolled?

Total	*Comp.*	*Deco.*	*Air*
67%	67%	64%	69%

b) Higher salaries would be available to the graduate upon completion of the correspondence course for which he enrolled?

Total	*Comp.*	*Deco.*	*Air*
44%	45%	38%	48%

c) Completion of the graduate's correspondence course would fully qualify him for a new or better job in the field?

Total	*Comp.*	*Deco.*	*Air*
64%	62%	70%	61%

(CX 279H) [85]

273. Twenty-five percent of the vocationally motivated graduate respondents to the RPC survey indicated that the possibility of higher salaries was a primary reason for taking the course; 42 percent indicated that the belief that the course would qualify them for a new or better job was a primary motivation; 54 percent indicated that their belief that new or better jobs would be available after completion of the course was a primary reason for taking it (CX 279H–I). The pertinent breakdown of the responses on this point was as follows:

What was the graduate's primary reason or reasons for taking the course?

	Total	*Comp.*	*Deco.*	*Air*
New or better job would be available after completing course	54%	53%	53%	56%
Higher salaries would be available after completing course	25%	28%	18%	29%
Completion of course would qualify me for a new or better job in the field	42%	39%	54%	36%
None of the above	8%	13%	7%	4%

(CX 279I)

274. Eighty-three percent of the graduate respondents to the

RPC survey indicated that they reached those beliefs because of the LaSalle representative or advertising or both (CX 279I).

275. The RPC survey findings on vocational experience may be summarized as follows:

(a) Those vocationally motivated graduates who never worked in the field of their course.

276. Almost two-thirds of all LaSalle Extension University graduates with vocational motivation indicated that they had never worked in the field of their course. Of that group, 64 percent indicated that [86]they did try to find a job in the field, but were unsuccessful. Of those who were unsuccessful in their job pursuit, 64 percent reported that the course they took was not recognized as adequate experience for the job they sought while an additional 30 percent indicated that a lack of jobs prevented them from securing employment in the field (CX 279I).

The breakdown by course of such responses is as follows:

Survey respondents who stated they never worked in the field of course

	Total	*Comp.*	*Deco.*	*Air*
Number	162	63	45	54
%	63%	67%	61%	60%

Survey respondents who stated they tried to find a job in the field of their course.

Total	*Comp.*	*Deco.*	*Air*
64%	42	28	34

Survey respondents who stated they did not try to find job in field of their course.

Total	*Comp.*	*Deco.*	*Air*
36%	21	17	20

Of those that tried to find a job, what they believe prevented them from securing the job they wanted or expected.

	Total	*Comp.*	*Deco.*	*Air*
Course not recognized as adequate experience	(104) 64%	25	20	22
Lack of jobs	30%	12	11	8
Inadequate salaries	7%	2	2	3
State of the economy	12%	4	2	6
Other	14%	8	3	4

(CX 279J) [87]

(b) Those RPC survey respondents who were vocationally motivated and were working in the field of their correspondence course at the time of enrollment.

277. Fifty-five (of the RPC respondents) indicated that they were working in the field at the time of their employment. Twenty-three of that group of 55 indicated that they had a new or better job *or* a higher salary. Fourteen of the 23 reported that the course did help them get a new or better job or a higher salary. Eleven respondents in the group indicated that they would not have gotten a new or better job *or* higher salary without having taken their correspondence course (CX 279J). Under RPC's definition of success, only the success of these 11 respondents was attributable to LaSalle (CX 279J).

The breakdown by course was as follows:

Those working in field at time of enrollment.

	Total	*Comp.*	*Deco.*	*Air*
Number	55	20	10	25
%	21%	21%	14%	28%

Those working in the field at time of enrollment and also working in the field at time of the survey.

	Total	*Comp.*	*Deco.*	*Air*
Number	32	14	5	13

Those working in the field at time of enrollment and at time of survey who stated they had a new or better job than when they enrolled.

	Total	*Comp.*	*Deco.*	*Air*
Number	17	7	4	6

Those working in the field at time of enrollment and at time of survey who stated they were earning a higher salary since completing course.

	Total	*Comp.*	*Deco.*	*Air*
Number	21	10	3	8

[88]Those working in field at time of enrollment and at time of survey who stated the course helped them get a new or better job or higher salary.

	Total	*Comp.*	*Deco.*	*Air*
Number	14	5	3	6

Those working in field at time of enrollment and at time of survey who stated they would not have gotten the new or better job *or* higher salary without the LaSalle course.

	Total	*Comp.*	*Deco.*	*Air*
Number	11	3	3	5

(CX 279K)

(c) Vocationally motivated RPC respondents graduating from LaSalle course not

working in the field of their course at the time of enrollment but working in field at time of survey.

278. New entrants into the field of their correspondence course comprise 12 percent of the total vocationally motivated graduate sample. This represents 32 [of the RPC] respondents.

Twenty-three of the 32 indicated that the job they now have is as good as the job they expected to get when they enrolled. Eighteen indicated that the salary that they are earning was what they expected to earn when they first enrolled for the course. Of those 24 individuals who indicated that their job *or* salary was what they expected when they first enrolled, 16 indicated that their course helped them to get their job or salary. Twelve respondents indicated they could not have gotten their job or salary without having taken the course. Based on the earlier definitions, RPC credited LaSalle Extension University with the success achieved by these 12 individuals (CX 279K–L).

The breakdown of responses on which this conclusion rests is the following: [89]

Those survey respondents who reported they were not working in field at time of enrollment but were working in field at time of survey.

	Total	*Comp.*	*Deco.*	*Air*
Number	32	7	14	11
%	12%	7%	19%	12%

Those survey respondents stating the job they now have as good as the job they expected to get when they enrolled.

23	5	11	7

Those survey respondents stating the salary they are currently earning was what they expected to earn when they first enrolled.

18	3	10	5

Of those whose job *or* salary was what they expected when they enrolled:

Those survey respondents who stated that what they learned in their course helped them get their current job or salary:

Total	*Comp.*	*Deco.*	*Air*
16	1	10	5

Those survey respondents who stated they would have gotten the current job *or* salary without having taken the course:

Total	*Comp.*	*Deco.*	*Air*
9	4	2	3

Those survey respondents who stated they would not have gotten the current job *or* salary without having taken the course:

Total	*Comp.*	*Deco.*	*Air*
12	0	8	4

(CX 279L)

279. On the basis of its definitions of success, RPC calculated the success rate of vocationally motivated graduates [90]in terms of the ratio of successful graduates to those entitled to expect success. This can be expressed as a fraction where the successful graduates are the numerator and those entitled to expect success, as a result of the LaSalle course, the denominator.

280. With respect to the vocationally motivated graduates in groups a, b, c (above) RPC found:

. . .197 of the 258 vocationally motivated graduates in the sample were identified as having pursued a vocational goal after completing their course. Of those who obtained a new or better job *or* a higher salary, and indicated that they could not have gotten either without having taken the course, the number is 23, or approximately 12%. On a course-by-course basis, the following matrix defines the success rate (CX 279L).

	Comp.	*Deco.*	*Air*
Total sample size of vocationally motivated graduates	94	74	90
Tried to find a new or better job or higher salary	71	56	70
Attained new or better job *or* higher salary	16	15	16
Could not have gotten new or better job *or* higher salary without having taken the correspondence course	3	11	9
Percentage of success attributed to LaSalle Extension University	4%	15%	10%

(CX 279M)[21] [91]

2. The CSI Analysis of the RPC Survey Data

281. Consulting Statisticians, Inc. (hereinafter cited as CSI) conducted an independent study of the data collected by RPC. The purpose of the study was to provide the FTC with an analysis of the success of vocationally motivated graduates of the LaSalle computer

[21] Complaint counsel does not propose that the finding be based on RPC's computation of the success rate. Rather they urge that the Commission adopt the recomputation of the RPC data on this point by Consulting Statisticians Inc. (CB p. 37).

programming, interior decorating and basic air conditioning and refrigeration courses (CX 1081C).

282. The computations by CSI made no attempt to compensate for possible bias in the underlying data (Atkinson 4361–62).

283. Critical to CSI's analysis was the formulation of a definition of success for LaSalle graduates who were vocationally motivated (CX 1081I–J).

CSI formulated three definitions of success:

> The broad definition on the basis of the RPC data is that students responding that after graduation they obtained a new or better job or a higher salary are successful.
>
> The narrow definition adds to the requirements for success that the student responded that the LaSalle course was instrumental in their vocational achievement.
>
> A definition based on expectations was formulated by restricting the candidates for success to those responding that they believed upon completion of their course that new or better jobs or higher salaries would be available to them (CX 1081J).

CSI made no judgment as to which was the best definition (CX 1081K).[22]

284. CSI judged separately those who were in the field at the time of enrollment and those who were not; this distinction was maintained because members of the two groups were likely to [92] encounter differences in job opportunities and success by virtue of their experience (CX 1081K). There were fewer cases of those working in the field at the time of enrollment than those who were not (CX 1081R–W).

According to the CSI computation, the success rate for graduates working in the field of the course at the time of enrollment was higher than for those not working in the field at the time of enrollment (CX 1081P).

285. In all courses, the broad definition yielded the highest success rate. The narrow and expectation based definitions tended to yield comparable rates and show no consistent pattern among their relative magnitudes (CX 1081P).

286. Overall, the key factor that differentiated the success rates of the three definitions was the requirement, in the narrow and expectation-based definitions, of a statement that the course helped in finding a new or better job or a higher salary. This requirement reduced the narrow and expectation-based rates relative to the broad definition rate (CX 1081P–Q). [93]

287. CSI computed the following success rates under the three definitions:

[22] Complaint counsel argues that the narrow definition should be adopted (CBp. 37; CRB p. 40).

Broad Definition of Success

	Computer Programming	*Interior Decorating*	*Air Conditioning/ Refrigeration*
Student working in field at time of enrollment	76.9%	80%	69.2%
Student not working in field at time of enrollment	15.1%	33.3%	24.3%
Aggregate	27.3%	37.7%	36%

(CX 1081R–T) [94]

Narrow Definition of Success

	Computer Programming	*Interior Decorating*	*Air Conditioning/ Refrigeration*
Student working in field of course at time of enrollment	38.5%	50%	50%
Student not working in field of course at time of enrollment	1.8%	21.6%	13.2%
Aggregate	8.9%	24.6%	23.1%

(CX 1081U, V, W) [95]

Definition of Success Based on Expectations

	Computer Programming	*Interior Decorating*	*Air Conditioning/ Refrigeration*
Student working in field at time of enrollment	33.3%	50%	50%
Student not working in field at time of enrollment	2.5%	26.5%	3.4%
Aggregate	6.5%	27.8%	13.5%

(CX 1081X–Z)

288. The extent to which the different definitions yielded numerically different success rates provides an indication of the inherent ambiguity in defining success (CX 1081 O). In the case of the narrow

definition, the ambiguities were resolved against LaSalle by CSI (Atkinson 4354).

289. The computer programming, interior decorating, and air conditioning courses do not represent a random sample of all the LaSalle courses and, therefore, it is improper to draw any inferences from such findings as to the success of LaSalle graduates in general (CX 1081 O–P).

3. Weight To Be Attributed to RPC Survey Data

290. Bias results in error in survey findings. Bias can be introduced through factors such as a faulty universe or sample, deficient analysis of the data, or the manner in which questions are asked in a survey (Chambers 145–48). Anything which suggests one answer as opposed to another has the potential for creating bias (*Id.* at 201). Put another way, bias relates to lack of reliability, validity and lack of accuracy (Atkinson 4256–57). There is some bias in all research (Chambers 148, 201); however, it is imperative to make the effort to avoid it (Zeisel 2580). [96]

291. As a general rule, covering letters for survey questionnaires should be as innocuous as possible so as not to bias those responding to the survey (Linden 4165; see also Chambers 203–04). Generally, the sponsor of a survey should not be noted where such indication could affect the nature of the responses (Linden 4166).

292. The original draft of the cover letter, utilized in the RPC survey of LaSalle, was submitted by RPC to the Federal Trade Commission and rejected. RPC was told by the Federal Trade Commission that it had to use the cover letter in evidence as CX 279CC. The initial sentence of that letter was drafted by the Federal Trade Commission (Chambers 204–05).

293. The cover letter of the RPC survey had a letterhead stating "Federal Trade Commission, Chicago Regional Office." The first sentence of the letter stated "The Bureau of Consumer Protection is gathering information from people who enrolled in LaSalle Extension University correspondence courses to determine if any action is warranted" (CX 279CC). The survey questionnaire itself was headed with the legend "Bureau of Consumer Protection Questionnaire LaSalle Extension University Graduates" (CX 279DD). The signatory of the cover letter was identified as a Federal Trade Commission attorney (CX 279CC).

294. The cover letter introduced bias on a number of counts. It was on Federal Trade Commission stationery and thus signaled that the survey was an inquiry under the auspices of the Federal government. The references to the Bureau of Consumer Protection

implied that LaSalle's students would require protection. This implication was reinforced by the statement in the letter that the survey was being conducted to determine if any action was warranted. The letter as a whole suggested that LaSalle was under investigation for illegal practices injurious to the consumer (Linden 4165–66; Zeisel 2455–56, 2508).[23]

295. The legend "Bureau of Consumer Protection Questionnaire" at the top of the questionnaire reinforced the suggestion inherent in the cover letter that LaSalle students might need protection (Zeisel 2457). [97]

296. The cover letter used in the RPC survey of North American Schools for the Federal Trade Commission did not contain such biasing elements. It was on the letterhead of RPC, mentioned the FTC only once in the body of the letter, and had no reference to an FTC attorney or to a determination of whether action would be warranted. There was no reference to the Bureau of Consumer Protection (RX 271RR; Zeisel 2457).

297. If the objective is to avoid bias, it is not good survey practice to use a cover letter and questionnaire indicating that the purpose of the survey is a law enforcement investigation.

RPC's failure to attempt to ascertain the direction of the bias inherent in the first sentence of the cover letter and the telelphone interview (Finding 294, n. 23) did not constitute good survey practice.

298. The cover letter created an atmosphere which increased the likelihood of response from dissatisfied students rather than from those students who had had a positive experience with LaSalle (Linden 4167; Zeisel 2455–56; see also Zeisel 2494–95). The increased likelihood of one group, as opposed to another, responding to a survey may be defined as self-selection (Zeisel 2456).

299. Persons with a grievance or a latent dissatisfaction are more likely to respond to a mail survey and thus select themselves (See Zeisel 2455–56, 2494–95). In a telephone survey, self-selection is for the most part obviated by the nature of the medium. The mail responses were generally less favorable to LaSalle than the telephone responses (Zeisel 2494–99, 2576–78; RX 257N–Q, 257HH).[24]

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[23] "[T]he leading sentence to that [in the cover letter] which was also the leading phrase during the telephone interview, does have a potential for bias" (Chambers 172). (RPC was told that this was required by law (Chambers 172).) The Commission's expert Dr. Chambers while acknowledging this potential for bias stated he did not know which way the bias goes and made no attempt to measure it (Chambers 172).

[24] Consider for example question 4 of the survey reading in pertinent part as follows:

> 4. Did LaSalle Extension University, either through its advertising material or its representative, lead you to believe that
>
> Yes No
>
> a. New or better jobs would be available to you in the field of your correspondence course upon completion of the course for which

(Continued)

The pattern of the mail-[98]telephone responses (RX 257) corroborates the opinion of respondents' expert that the cover letter had the potential for introducing bias by self-selection. [99]

300. Over and above the question of self-selection, the cover letter's suggestion that LaSalle was the subject of a law enforcement investigation and the implied suggestion of wrong doing contained therein was likely to bias, in a manner adverse to LaSalle, the responses to the survey (Zeisel 2456).

301. The decisive bias in the RPC survey was the psychological attitude or emotional feeling of students or ex students toward the school. There was no objective test which would measure this type of bias (Linden 4169–70, 4210).

302. The effect of the bias inherent in the cover letter and the legend "Bureau of Consumer Protection" on the questionnaire of the RPC survey was compounded by the fact that questions concerning subjective issues, such as the students' motives in enrolling and their

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you enrolled	[ ]	[ ]
b. Higher salaries would be available to you upon completion of the correspondence course for which you enrolled	[ ]	[ ]
c. Completion of your correspondence course would fully qualify you for a new or better job in that field	[ ]	[ ]

In the context of this survey "yes" answers to question 4a, b, and c were adverse to respondents; conversely "no" responses were favorable to LaSalle.

The record shows the following differences in the rate of "yes" and "no" responses between mail and telephone respondents.

		Non-graduates		*Graduates*	
		Mail	*Telephone*	*Mail*	*Telephone*
4(a)	Yes	68.2%	70.5%	57.7%	50.6%
	No	13.6	23.1	29.0	44.4
	N/R	18.2	6.4	13.4	4.9
		(RX 257D)		(RX 257P)	
4(b)	Yes	51.7	60.3	34.9	35.8
	No	19.3	32.1	41.1	59.3
	N/R	29.0	7.7	24.0	4.9
		(RX 257E)		(RX 257Q)	
4(c)	Yes	69.9	70.5	56.2	58.0
	No	13.6	25.6	31.7	42.0
	N/R	16.5	3.8	12.1	0.0
		(RX 257F)		(RX 257R)	

The tabulation shows that the percentage of "yes" answers by telephone respondents exceeded the percentage of "yes" answers given by the mail respondents to a number of questions. It is, nevertheless, clear that in the case of each question the percentage of "no" answers given by telephone respondents is significantly larger than the percentage of "no" answers of mail respondents to the same question. Moreover, in the case of every question, the percentage of respondents listed as giving no response is substantially higher in the mail than the telelphone category. In the case of every question, the percentage increase of "no" answers by telephone over "no" mail responses significantly exceeds any similar increase in the case of "yes" responses. Accordingly, the inference may be drawn that answers to the questions by those mail respondents, in the no response category would be likely to be more favorable to LaSalle. The overall pattern of respondents to Question 4 therefore supports expert opinion that the survey had the potential for increasing self-selection; respondents hostile to LaSalle would be more likely to respond.

impressions of representations made to them at the time of enrollment, in the case of a third or more of the graduates, related to events three to four years or more prior to the time of the survey (Colloquy Tr. 115, 125; see Linden 4176).

303. A number of key questions in the survey were leading in a manner adverse to LaSalle. For example:

Did LaSalle Extension University, either through its advertising material or its representative, lead you to believe that: [100]

(a) New or better jobs would be available to you in the field of your correspondence course upon completion of the course for which you enrolled?. . . (CX 279DD)

As phrased the question suggested the survey respondents were "led. . .to believe" that the following benefits would be derived from the correspondence course (a) a new or better job, (b) a higher salary, or (c) completion of the course would "fully qualify" the graduate for a new or better job in the field." The suggestion inherent in questions 4a, b, and c was augmented by the fact that no alternative was offered to a, b, or c.[25] The question was weighted against respondent.

Moreover, the suggestion inherent in the question was compounded by the effect of the cover letter (Findings 298–300).

304. Because of the interval between the events surveyed and the date of the survey, RPC's failure to include alternative answers of "I don't know" or "I don't remember" may have biased the results. The lack of alternatives forced respondents to the survey to check one of the precoded answers (Zeisel 2461–62, 2483).

305. RPC's precoding[26] of certain questions had the potential for introducing bias. The first question concerning the crucial issue of motivation provided three choices as follows:

People take a correspondence course for a variety of reasons. Which statement [101] below best explains your personal reason for taking the correspondence course you did?

a. To improve my vocational opportunity by getting a new or better job or a higher salary

b. To learn something new or useful, but not to get a new or better job or a higher salary

c. Other, please specify (CX 279DD).

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[25] Question 4(d) asked: "Which of the above, if any, was the primary reason or reasons you enrolled for the course? (answer as many as apply)" As a practical matter, the choice "none of the above" in subpart (d) is really not a choice at all since the survey respondent is only instructed to fill out that subpart to Question 4 if he has already answered "yes" to a, b, or c (CX 279DD).

[26] Precoding is the list of multiple choice answers provided for a given question (Zeisel 2509).

A respondent choosing response (a) would be classified as a vocationally motivated student (Chambers 214).

306. The formulation of choices "a" and "b" in question 1 tended to maximize the number checking "a" indicating vocational motivation alone in enrolling in the LaSalle courses. A respondent to the survey with any vocational motive, although slight in comparison to other reasons, was in effect forced to choose "a" over "b" (Linden 4183–84; Zeisel 2458–60). The precoding in this question had the potential for bias since write in answers such as "c" as a general rule receive little response (Zeisel 2458).

307. The list of reasons provided for enrolling by question 1 is unusually lean (Zeisel 2460). Generally, a number of elements go into such a decision and had more options been provided it is likely that there would have been fewer occupationally oriented responses (Linden 4184).

308. In a previous survey of Bell and Howell conducted for the FTC, RPC had distinguished between primary and secondary reasons for enrolling in a correspondence course (Zeisel 2460). In the case of the Bell and Howell questionnaire, the question designed to elicit the reasons for enrollment was formulated with a wider range of choices. The first category was "to get a job in a new or different field;" the second was "to get a better job in the same field;" the third was "to do my job better and to upgrade my skills;" the fourth was "to learn something new or useful but not to get a better job" and the fifth was "if other please specify" (Chambers 215–16).

The two largest responses received to this question in the Bell and Howell survey were "to do my job better to upgrade my skills" and "to learn something new or useful, but not to get a new or better job" (Chambers 216). [102]

309. The phrasing of the question concerning the motivation for enrollment in the LaSalle survey in effect eliminated the choice "to do my job better, to upgrade my skills" (Chambers 219;[27] CX 279DD).

The result of eliminating this alternative was to force survey respondents to choose between saying that their primary motive was to get a job or salary increase, and indicating that they did not intend to get a new job or salary increase (Chambers 220–22).

310. The precoding in question 1 of the RPC survey, accomplished by narrowing or "collapsing" the choices in question 1 of the Bell and Howell questionnaire, had the potential to bias the survey results by affecting the success ratio adversely to LaSalle. The precoding in the

[27] Q. , . .How did you find either doing my job better or upgrading my skills, where is that found in 1-A of the LaSalle questionnaire?

A. Well, its an interpretative point for us. We felt it was a logical collapse (Chambers 219).

LaSalle questionnaire by narrowing the range of choices and "forcing" a choice on the survey respondents had the tendency to maximize those respondents classified as having a vocational motivation (Findings 305–09; Zeisel 2458–60; Linden 4183–84). As a result, the denominator of the success ratio may have been unduly expanded (See Linden 4183–85).[28]

311. Questions 5–13 of the questionnaire, designed to measure the success of LaSalle graduates, limited the definition of success to "the field of your correspondence course" (CX 279EE; Zeisel 2477–80, 2508). The exclusion of "in a closely related field" from the measure of success precluded, for example, consideration of the benefit of a salary increase **[103]**attributed to a LaSalle course in a field closely related to the field of training (*E.g.,* Krider 2836–42, 2845, 2849–55).

312. In the Universal survey, conducted for the FTC by RPC, the measure of success was defined in terms of "in the field of your correspondence course or in a closely related field" (Zeisel 2477–78).

313. Excluding consideration of vocational benefit in a closely related field tends to decrease the number of graduates in the numerator of the success ratio and thus diminishes the measure of success calculated from that fraction.

314. The arrangement of precoded answers so that the answer least favorable to LaSalle was frequently placed first had the potential to bias the results of the survey. There is a tendency by survey respondents to check the first alternative in the case of multiple choice answers (Zeisel 2461–64). To avoid such bias, it is good practice to rotate the precoded answers on the questionnaires sent out (Zeisel 2462, 2464).

315. The RPC questionnaire did not measure degree of dedication in seeking a job, *i.e.,* number of employer contacts made in seeking employment (Linden 4194). For that reason, it is difficult to determine, on the basis of this survey, how much credence to give to reasons given by respondents for not getting a job after taking the course (See Question 14, CX 279EE).

316. Question 4 in the RPC survey questionnaire was an attempt to determine the vocational expectations raised by LaSalle's advertising and/or its representatives.[29] **[104]**

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[28] ". . .we have this number of people here who may not have had as a prime reason an occupational aspiration, and hence in the subsequent questions will reflect a kind of behavior which accrues to the school negatively. In other words, they would not have been able to find a job if, in fact, they were not really, really occupationally interested or oriented since they were not going to pursue it that diligently" (Linden 4185).

[29] 4. Did LaSalle Extension University, either through its advertising material or its representative, lead you to believe that

	Yes	No
a. New or better jobs would be available to you in the field of your correspondence course upon completion of the course for which you enrolled	[ ]	[ ]

(Continued)

317. The phrase in that question "lead you to believe" in the context of the impression created by the cover letter that LaSalle was the subject of a law enforcement inquiry (Findings 292–95) had the tendency to bias the response to that question (See Zeisel 2465; Linden 4172–73).

318. The effect of leading questions in the survey adverse to LaSalle was compounded by the biasing effect of the cover letter and heading of the questionnaire.

319. A number of changes which distinguish the RPC survey of LaSalle from preceding surveys of other correspondence schools conducted for the FTC by the same survey organization tended to diminish LaSalle's success ratio as computed on the basis of the instant survey (Findings 296, 308–13).

320. The CSI retabulations are affected by the bias inherent in the RPC survey instruments (Finding 282).

321. Neither firm conclusions or confident findings can be based on the RPC survey.

B. The Veterans Administration Surveys

322. Public Law 93–508 requires, for continued Veterans Administration (hereinafter cited as VA) approval, a showing that 50 percent of the persons completing a vocational course were placed in employment in the field for which the course was designed or in a closely related occupation (RX 206). Such surveys were a requirement for all courses certified by the VA for reimbursement to veterans (Hetzel 3131). LaSalle conducted VA surveys of its graduates in 1975 and 1977 (RX 201, 205; Hetzel 3130–31). [105]

323. The VA procedures required schools to survey all graduates or a random sample of graduates (if there were more than 300 graduates in a particular course in the two year period). The questionnaire form which was prescribed by the VA asked graduates whether they had, since completing the course, worked in an occupation "directly related" or "closely related" to the course. If both questions were answered in the negative, the graduates were further asked if they had been available for employment in the field for which training was taken (RX 201K, 205P).

324. The final figure on the survey was an employment percentage or "employment rate" for each course which was calculated by

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b. Higher salaries would be available to you upon completion of the correspondence course for which you enrolled [ ] [ ]

c. Completion of your correspondence course would fully qualify you for a new or better job in that field [ ] [ ]

adding the graduates who responded that they had worked in positions "directly related" or "closely related" to their training, and dividing by the number of graduates who responded less those stating they had not been available for employment (RX 201M, 205Q). A minimum employment percentage of 50 percent based on this figure was required to obtain or maintain VA approval for purposes of reimbursement (RX 201B, 205B).

325. LaSalle first determined the number of graduates in each of the courses involved for the period under consideration, and selected by sample the number of graduates in each course to meet the VA requirements as to count. LaSalle then mailed to each individual in the sample group the required questionnaire form. It did a follow-up mailing as required by the VA, and where that failed to produce a response, LaSalle made at least three telephone attempts pursuant to the VA instructions to secure the data required to fill in the form (Hetzel 3132).

326. The VA surveys asked students to respond whether since completing the course they had worked in an occupation directly related to this training or whether the respondents to the survey since completing the course had "worked in a closely related job, comparable in level to the type of work for which this course provided training" (RX 201K). The determination of what was a closely related job was left to the students (Hetzel 3134–35).

327. The VA surveys did not take into account whether or not a person was working in the field of his training prior to the time he enrolled in the course (Hetzel 3179).

328. The 1975 VA survey conducted by LaSalle was subject to a government audit which lasted two weeks (Hetzel 3147–48; RX 253). Among the courses audited were basic computer programming, interior decorating, and basic air conditioning and refrigeration (RX 253).

329. LaSalle had submitted forms to the Veterans Administration for 18 courses showing at least a 50 percent employment rate in the same or closely related type of work. The audit for three of the courses showed that they did [106]not meet the 50 percent employment criterion (RX 253L). The courses in which enrollments were suspended as a result of the audit were Complete Law Training, Hotel/Motel Executive Training, and Interior Decorating (RX 253K).

The audit report concluded as follows:

> This audit revealed that the school had made some mathematical errors in computing the results of their surveys and that their procedures could be improved; but, the discrepancies found do not appear to be willful attempts to alter the results of the surveys (RX 253L).

330. The final percentages from the VA 1975 and 1977 surveys, for the computer programming, interior decorating, and air conditioning courses, after downward revision by VA auditors and by counsel[30] were as follows:

Course	*1975 (Survey)*	*1977 (Survey)*
Computer Programming (CX 282J, 288)	58.5%	43.8%
Interior Decorating (RX 253H, 279)	47.5%	49.5%
Air Conditioning and Refrigeration (CX 282R; RX 277) [107]	56.6%	52.7%

1. LaSalle's Adjustment of 1975 VA Survey Figures

331. In the 1975 VA survey, LaSalle asked an additional question of those respondents who were not employed in their field of training but who had stated they were available for employment. Such graduates were asked whether they had contacted employers in an effort to secure jobs (RX 202).

332. Respondent adjusted the success rate by eliminating from the candidates for success those who had not looked for employment. The following is a comparison of the adjusted and unadjusted figures for three of the courses:

	Unadjusted (CX 282)	*Adjusted* (RX 203)
Basic Computer Programming	58.5%	69.6%
Interior Decorating	50.6%[31]	54.4%
Air Conditioning and Refrigeration	56.6%	66.7%

C. LaSalle's 1974 Graduate Survey

333. LaSalle conducted a mail survey of its graduates in November and December 1974. A questionnaire was mailed once to every student who had graduated in the first six months of 1974 (Hetzel

[30] The adjustments involved a review of the responses concerning jobs in a field "closely related" to the field of training. Where job titles and description of jobs indicated that jobs were not so related in the reviewers' opinion, the responses were reclassified. The 1975 audit figure in the case of the interior decorating course was revised by VA auditors (RX 253). The 1977 VA survey figures were reviewed and revised separately by complaint counsel and respondents' counsel. Set forth here are respondents' revisions which are somewhat lower than those of complaint counsel (Stipulation October 23, 1979; RX 277, 279).

[31] The VA audit (Findings 328–30) reduced the unadjusted figure for interior decorating from 50.6 percent to 47.5 percent (RX 253H) applying the same correction to adjusted figure the latter becomes 51.3 percent.

3142-43; RX 214A-B). The combined response rate for all [108] courses, excluding the high school program was approximately 37 percent (Zeisel 4130, 4149; RX 215, 254B).[32]

334. Over 90 percent of those who responded said they were satisfied with their course. Eighty-eight percent responded they would recommend the LaSalle course to others (RX 215B). These figures relate to all courses except the high school course.

The figures for the computer programming, air conditioning and the interior decorating course were as follows:

	General Satisfaction	*Willingness to Recommend Course*
Computer Programming	79.1%	66.7%
Air Conditioning	79.1%	71.9%
Interior Decorating	94.5%	90.1%

(CX 285-87)

D. Active Student Surveys

335. LaSalle made several mail surveys of its active students at irregular intervals. Such surveys were conducted in September and October 1974; a second survey was made in 1977 (Marshall 3215-16, 3220-21; RX 217).

336. In the 1974 survey of all courses, except the high school program, 96 percent of the respondents stated that up to that point, the course delivered what they expected; in the 1977 survey, the corresponding figure was 95 percent (RX 218C, 222H). [109]

E. Student Testimony concerning the Vocational Value of LaSalle's Correspondence Courses

337. In addition to the surveys, student testimony was offered into evidence concerning the vocational value of LaSalle's courses. The LaSalle students who testified with respect to the interior decorating, computer programming, and air conditioning courses had varied vocational success; their testimony will be reviewed on the issue of little or no worth.

1. Student Testimony about the Vocational Value of LaSalle's Interior Decorating Course

[32] LaSalle received 1581 responses and sent questionnaires to 4224 graduates (Zeisel 4130).

338. Of those students in the field of interior decorating who had had no prior education or experience in the field a number were successful in obtaining employment as interior decorators or in related fields or, in applying the skills they learned from LaSalle in the positions they held at the time of enrollment with LaSalle, or in starting their own business (Schaefer 2150–52, 2158; Haselden 2190, 2192, 2199; Perekovich 2392–94, 2403–18; Niemeyer 2718, 2727–29; Murphy 2761–62; Tuma 2781, 2783; Wright 2865–67, 2873, 2878–80; Miller 2925, 2932; Visser 2940–41; Sellers 3256–57, 3262; Ostland 3488, 3495, 3497, 3504; Kuster 3671–73, 3680; Corey 3777–78, 3783–84).

339. The majority of the LaSalle interior decorating graduates who testified had no prior education or experience in the field. Some students, for example, Charles Kohlmyer, had acquired knowledge in related fields prior to enrolling with LaSalle. Although Mr. Kohlmyer had no interior decorating education or experience as such, his prior education in architectural engineering must be considered as related to interior decorating. Mr. Kohlmyer's background, not typical of the ordinary LaSalle student, was no doubt an advantage in his career as an interior decorator (Kohlmyer 3336, 3357–58).

340. Some students, with no prior experience or education in decorating, directly attributed their vocational success in interior decorating to the LaSalle course (Murphy 2776; Wright 2873; Miller 2932). Other students acknowledged that the LaSalle course had been helpful in their work as decorators (Brooks 2698; Tuma 2787–90).

341. Not all of the students testifying with respect to the interior decorating course had been successful in obtaining employment in the field (Muhar 441, Seliga 1251, 1268–71; [110]Templin 1454–55, 1476–78); some students dropped out because they believed they would not be able to achieve their vocational goals with the LaSalle interior decorating course (Patrone 1759–61, 1785). Of those LaSalle interior decorating graduates who testified they were successful in obtaining employment, a number were not involved in a full-line decorating business but were employed in related fields (Schaefer 2154, 2158, 2176 [husband's carpeting business expanded to include wall coverings and draperies]; Haselden 2190 [Gloria's Bath Boutique]; Visser 2940–41 [husband's business in major appliances, hardware, paint and wall paper]; Kuster 3671 [furniture sales]).

2. Student Testimony about the Vocational Value of LaSalle's Computer Programming Course

342. Students enrolled in LaSalle's computer programming course reported varying degrees of success in obtaining employment

as programmers or programmer trainees (Compare Mull 340–47; Pichauffe 1657–58, 1669; with, Wilson 3273–74; Bashista 3529).

343. The two student witnesses who did succeed in obtaining programmer jobs had had some exposure to computers; they had not had any experience in writing programs (Wilson 3269–70, 3273–74, 3278–79; Bashista 3510–13, 3523–24). Ronald Douglas Wilson believed that he received a promotion from operator to computer programmer as a result of the LaSalle course (Wilson 3273–74).

344. Other students did not reap the benefits they anticipated from LaSalle's computer programming course. Neither Bruce Mull nor Lynn P. Pichauffe was able to obtain employment as a computer programmer or computer programmer trainee after graduating from LaSalle (Mull 340–46; Pichauffe 1669). Charles Edward Cline found that LaSalle's computer programming course was not acceptable as continued education for United States Army personnel purposes (Cline 1053–55, 1058–59, 1062–63).

3. Student Testimony about the Vocational Value of LaSalle's Air Conditioning and Refrigeration Course

345. Students with diverse backgrounds enrolled in the LaSalle air conditioning and refrigeration course. Some [111]students had no prior experience or training in the field (for example, Smith 3263–66; Palmer 3895–96; Martin 3941–42); others had some exposure to the servicing of air conditioners and refrigerators or experience in a related field (Diller 1103–04; Potter 2292–94; Sprout 2359), and others had previous training in the field (Waller 652–53, 655; Hanger 2620–23).

346. The previous experience or training of some students had no correlation to their success in obtaining employment in the air conditioning and refrigeration field after completing the LaSalle course. David Diller, who had had some prior experience in the field with the Coast Guard before enrolling in the LaSalle course and who after completing LaSalle's course received an AA degree as an Appliance and Refrigeration Technician, could not find a job as an air conditioning serviceman (Diller 1113–17). In addition, David Waller, John M. Kammer and Robert Dovenbarger testified that they did not secure employment as air conditioning and refrigeration servicemen after taking the LaSalle course (Waller 651, 668–75; Kammer 885, 894–96, 901; Dovenbarger 1481, 1487–92, 1497–99).

347. In contrast, a number of LaSalle graduates reported that they were successfully employed in the field of air conditioning and refrigeration repair after taking LaSalle's course (Hanger 2617; Potter 2298–99; Smith 3287; Palmer 3895–3903; Martin 3939). Some

graduates had opened their own repair shops (Hanger 2617; Potter 2298–99; Smith 3287).

F. Expert Testimony as to the Vocational Value of LaSalle's Correspondence Courses

348. Educators and employers testified about the vocational value of LaSalle's interior decorating, computer programming and air conditioning and refrigeration course.

1. Expert Testimony concerning the Vocational Value of LaSalle's Interior Decorating Course

349. Expert opinion in the record indicates that the materials in the LaSalle course covered the basics of interior [112]decorating on a fundamental level (Genis 3401–02, 3427–28).[33] The LaSalle course provided "basic knowledge—essential and fundamental, but no more" and the course while "it offers exposure" would not "make one an Interior Designer" (Letter Arline Genis to Respondents' Counsel May 1, 1979; CX 1032). According to expert opinion, experience in the field was essential or desirable in the training of interior decorators for more advanced or sophisticated levels (Walker 530; Genis 3438–39, 3445; Rankin 1340). In the words of respondents' expert, those LaSalle graduates who "would pursue [interior decorating] careers would find it necessary to have continuing education in the field" (CX 1032).

350. The ordinary and typical LaSalle graduate without some practical experience would not be qualified to open his own full line decorating service (Walker 527–28, 530; Rankin 1339–40; see also CX 1032).

351. Most experts or employers agreed that the LaSalle interior decorating graduates without further training or experience would be best qualified for a retail sales position (Lewis 429; Walker 535; Rankin 1344–45; Wimbush 3034–35).

2. Expert Testimony concerning the Vocational Value of LaSalle's Computer Programming Course

352. The LaSalle computer programming course was reviewed by several experts in the field of computer programming education. One expert found the course to adequately serve as an introduction to data processing with COBOL (Hamblen 1189, 1192, 1235–36). Another

[33] Respondents expert Arline Genis stated in this connection "And when I say basic and fundamental, I mean just that. It opens up the curiosity. . . It does not in any way prepare for a total career. But it is a good introduction I think" (Genis 3428).

expert was of the view that the LaSalle course gave a good representation of the basic principles on which computers work (Safford 3567). The course's primary problem in achieving the course objectives was the lack of opportunity for a student to run a program through a computer and then to check for errors (Engel 977, 993; Hamblen 1202, 1236).[113]

353. Graduates of the LaSalle course would have an advantage in securing various semi-clerical positions in the data processing field because of familiarity with the terminology (Hamblen 1208–09) or in gaining acceptance into a training program for computer programming (Safford 3601); they would not qualify as beginning programmers (Hamblen 1208–09, 1247–48; Engel 1001–02).

3. Expert Testimony concerning the Vocational Value of LaSalle's Air Conditioning and Refrigeration Course

354. Although the LaSalle course would not qualify the ordinary graduate as a mechanic, the course did provide knowledge of the fundamental principles of air conditioning and refrigeration (Laham 732;[34] Wintersdorf 1522, 1525; Lupson 3998–99).

355. The major drawback to LaSalle's course was the lack of hands-on experience (Laham 735–36; Ritchie 1084; Wintersdorf 1525–26, 1551–52). A student, with no training or experience other than LaSalle would be qualified to enter the field as an apprentice[35] (Laham 735; Lupson 4090; Wintersdorf 1525). Although such a graduate would be qualified to handle simple problems he would need supervision (Laham 715, 718–19, 726–27; Lupson 3998–99) and would therefore not qualify as a mechanic or fully qualified serviceman (Lupson 3999; Laham 733). Moreover, hands-on experience may play an important role in choosing apprentices or trainees in a field which may be overcrowded (McCarty 625–26, 630–31; Ritchie 1090–91; Lupson 4089–90). [114]

VIII. Respondents Had Notice That Certain of Their Representations May Have Been Misleading and Unfair

A. Demand Representations

356. In August 1975, respondents submitted their self-evaluation report to the NHSC (CX 327). In that report, respondents included

[34] "From an introductory point of view, as far as basic knowledge goes it [LaSalle's treatment of air conditioning and liquid chilling systems] was handled very well. As far as teaching a man to go in and become a mechanic, I don't feel it was in depth enough" (Laham 732).

[35] "An apprentice will always be supervised by a mechanic or shopman or somebody to insure that what they are doing is proper and what we have requested of them" (Lupson 3999).

an outline of the course objectives for the computer programming course.

357. In December 1975, the report of the Chairman of the NHSC Accrediting Commission found that "the educational objective for Basic Computer Programming, *i.e.*, to provide the student with a basic coding skill at the level to be considered for a position as a computer programmer trainee, is not met by completing the course" (CX 328A, H, K).

358. On January 31, 1976, the NHSC Accrediting Commission, with the notice of reaccreditation, transmitted the following specific criticisms of the LaSalle Computer Programming Course:

I. 2 Appropriate Objectives—The student does not acquire a job skill at the level to be considered for a position as a computer programmer trainee.

II. 1 Comprehensive Instructional Materials—The programming language (COBOL, RPG, FORTRAN IV) instructional materials do not provide the in depth coverage required to train a student to code and/or modify a program.

III. 1 Examination Service—The COBOL language exams (Volumes III and IV) and the optional RPG and FORTRAN IV exams are unsatisfactory. The majority of questions are multiple choice, and do not test the student's ability to code and test the coded problems on the computer. Separate exams should be given for all lessons in Volumes III and IV.

I have never taken, or taught, or heard of a programming course that does not have the student write at least one program. The examinations in [115]this course are entirely multiple choice and do not provide the student with the coding experience that he needs. Grading coded programs are (sic) considerably more difficult than grading multiple choice questions but nevertheless the student at least needs to know if his coding would work if it were placed in a computer. This would also eliminate the chance of the student scanning the textbooks for the "key answer," since there are no "key answers" in coding a program.

The course objectives are also vague. The booklet states that "this training, combined with the graduates personal ability, prepares him to enter the field as a Computer Programmer Trainee. . ." Yet it also states that "It takes training and experience to handle the programming assignments. . ." The brochure generally implies that the student should be able to acquire a job as a Computer Programmer Trainee upon completion of the course. In today's economy, this seems overly optimistic.

Recommendations—if the technical material were toned down, this would be an excellent course for non-EDP personnel who either come in contact with computer reports on peripheral basis or must discuss problems with EDP personnel and desire a better working knowledge of computer terminology and programming. Under this format, there would not be a requirement, as I believe currently exists under the present format, for a computer in order to meet the proposed course objectives (CX 330A–B, D–E).

359. In the same period, respondents were on notice, as a result of the accreditation process of NHSC, that the LaSalle interior

decorating graduate with no further training might not be able to achieve the objectives for that course (CX 328H) and that the respondents' course objectives for that course did "not reflect an awareness of nor state the necessity for actual on-the-job mastery" (CX 328K).

360. In the same period, respondents were put on notice, through the NHSC accrediting process, that graduates of the air conditioning and refrigeration course might not be able to fulfill the vocational objectives of that course. LaSalle was advised that although the course is basic, "it seems necessary to provide hands-on training kits to novices who enter a [116]technical field where maintenance and servicing of equipment, to some extent, must be practical vocational objectives" (CX 328L).

361. Respondents as a result of the comments of the NHSC accrediting committee were put on notice that, absent further training, the course objectives of the interior decorating, computer programming, and air conditioning courses might not be met, and that as a result their representations regarding the vocational qualifications of graduates in those courses may have been misleading.

362. The notice to respondents that their representations as to the qualifications of graduates of those courses may have been misleading also put respondents on notice that their representations as to the demand for and earnings potential of such graduates may have been deceptive.

B. Selectivity

363. Respondents' advertising and promotional claims had the tendency to create the impression that, over and above standard minimum age and educational requirements, students were screened for aptitudes necessary or helpful to successful completion or assimilation of particular courses (Findings 275). Since respondent did not screen for such aptitudes (Finding 256), it should have known such representations were misleading.

C. Cancellation and Tuition Refund

364. Respondents knew or should have known that the failure to disclose material facts concerning their cancellation and refund policy was misleading and unfair (Findings 211–13, 222–23). [117]

Discussion

The complaint charges Macmillan, Inc. and its wholly-owned subsidiary, LaSalle Extension University, with violation of Section 5 of the Federal Trade Commission Act. Respondents, it is alleged, have committed unfair acts and practices in connection with the offering for sale and sale of correspondence courses in commerce.

The violations charged are not novel. They involve allegations that the demand for and earnings potential of graduates of LaSalle's courses have been misrepresented. The complaint further alleges that respondents misrepresented that their graduates would be qualified to secure employment in the fields for which they trained without further training and experience, and that prospective students would be screened to determine that they had the qualifications and ability to successfully assimilate and complete respondents' courses.

Other charges allege that respondent had no reasonable basis to support the representations concerning the demand for their graduates in the fields for which they trained.

The complaint also charges that respondents have disparaged the potential career opportunities, education and self-image of prospective students in conjunction with representations that LaSalle's correspondence courses could improve their personal characteristics. Such disparagement, it is alleged, aggravates the deceptive and unfair effect of other representations and is therefore unfair.

Other allegations charge that respondents misrepresented or failed to disclose the true nature of the financial obligation incurred when the contract was signed and that they induced prospective students to execute enrollment contracts without affording sufficient time to consider such purchase.

Finally, respondents are charged with unfairness in failing to refund tuition when payment was induced by unfair or deceptive acts and the courses were of little value in fulfilling the expectations raised by respondents' representations.

The issues to be resolved after trial run the gamut of the charges in the complaint. Without repeating the details of the charges, it is evident that the basic issue is the proper construction of respondents' advertising and promotional materials as well as statements made in the course of the sales presentation. In that connection, it must be determined whether respondents have failed to disclose material facts in their promotion of the courses. [118]

Most of the litigation effort herein was expended on the issue of restitution. Respondents challenge the Commission's authority to

order restitution in an administrative proceeding pursuant to Section 5 of the Federal Trade Commission Act. In addition, respondents claim that complaint counsel have not met their burden of proving that the courses were of little or token value for the purposes for which they were taken.

I. Construing Respondents' Promotional and Advertising Claims To Ascertain the Representations Made

The proper construction of respondents' advertising and promotional claims is a major issue. The following general principles apply to the interpretation of the advertisements under consideration.

Proof of actual deception or intent to deceive is not prerequisite to establishing a violation of Section 5 of the Federal Trade Commission Act. Misrepresentations are condemned if they possess a tendency to deceive. *Trans World Accounts Inc.* v. *FTC,* 594 F.2d 212, 214 (9th Cir. 1979); *Resort Car Rental System Inc.* v. *FTC,* 518 F.2d 962, 964 (9th Cir.), *cert. denied, sub nom. MacKenzie* v. *United States,* 423 U.S. 827 (1975); *Montgomery Ward & Co.* v. *FTC,* 379 F.2d 666, 670 (7th Cir. 1967).

Consumer testimony is not required to establish a violation.[36] "[T]he Commission may draw its own inferences from the advertisement and need not depend on testimony or exhibits (aside from the advertisements themselves) introduced into the record" *Carter Products Inc.* v. *FTC,* 323 F.2d 523, 528 (5th Cir. 1963). *Resort Car Rental Systems* v. *FTC,* 518 F.2d 962, 964 (9th Cir. 1975); *Royal Oil Corp.* v. *FTC,* 262 F.2d 741, 745 (4th Cir. 1959).

The test of whether promotional materials and advertisements are false and misleading is the overall impression they are likely to make on the buying public. *Carter Products Inc.* v. *FTC,* 323 F.2d 523, 528 (5th Cir. [119]1963); *Murray Space Shoe Corporation* v. *FTC,* 304 F.2d 270, 272 (2nd Cir. 1962); *Charles of the Ritz Distr. Corp.* v. *FTC,* 143 F.2d 676, 679 (2nd Cir. 1944).

In its review of advertising, "[t]he Commission is concerned with protecting the trusting as well as the suspicious, the casual as well as the vigilant, the naive as well as the sophisticated." *Colgate-Palmolive Co.,* 59 F.T.C. 1452, 1464 (1961), *vacated and remanded,* 310 F.2d 89 (1st Cir. 1962), on remand from First Circuit 62 F.T.C. 1269 (1963), *vacated,* 326 F.2d 517 (1st Cir. 1963), *rev'd,* 380 U.S. 374 (1965).

[36] Although some student witnesses did testify about their impressions of LaSalle's promotional scheme, the deception issue has been resolved primarily on the basis of LaSalle's advertisements, course brochures, and standard sales presentation. In addition, the opinions of experts have been considered in evaluating the qualifications of graduates for employment.

A. Respondents' Representations As to the Demand for, Qualifications of and Earnings Potential of Their Graduates

Respondents' advertising and promotional materials were part of a total scheme to market LaSalle's courses in which the pervasive theme was success through LaSalle. In connection with that theme, respondents represented that there was a need or demand for LaSalle graduates, that LaSalle graduates could expect to earn high salaries, and that typical and ordinary LaSalle graduates would be qualified to enter the field for which they were trained with no prior education or further experience or training (Findings 88, 91, 92–119, 132–54, 172–93). The ordinary and typical LaSalle graduate did not have the qualifications represented and such claims had the capacity to deceive (Findings 120–31, 155–71, 194–99).

The above mentioned representations were conveyed at successive stages of respondents' contact with prospective students beginning with the advertisements, continuing with a brochure mailed to the prospect, and concluding with a LaSalle representative's sales presentation (Finding 88). The evidence pertaining to these representations and the allegations that such representations were false and misleading related to LaSalle's computer programming, interior decorating and air conditioning and refrigeration courses.

In a number of instances (CX 4A, 5A, 6A, 8A; RX 20), respondents affirmatively represented that LaSalle graduates would be able to earn higher salaries and meet the qualifications required for certain positions. For example:

> What does it take to earn higher pay? First, pick an uncrowded field where you have the chance to move ahead fast. Second, prepare with the right training—LaSalle training (CX 5A). [120]

In other instances, the point was made indirectly through use of testimonials which implied that the success portrayed therein was ordinary and typical for LaSalle graduates (Finding 89).

A deceptive impression may be created by implication and innuendo without affirmative misrepresentation or misstating a single fact. *Baker Franchise Corporation* v. *FTC,* 302 F.2d 258, 261 (3d Cir. 1962); *Feil* v. *FTC,* 285 F.2d 879, 896 (9th Cir. 1960); *Aronberg* v. *FTC,* 132 F.2d 165, 167 (7th Cir. 1942). Respondents use of testimonials had the capacity to deceive.

Once a misleading overall impression has been created, as in this case by LaSalle's repeated reinforcement of the success through LaSalle theme in numerous advertisements, course brochures and through its sales representatives, explanations, disclaimers, or caveats are not likely to save the consumer from being misled.

Waltham Precision Instrument Co., Inc., 61 F.T.C. 1027, 1047 (1962), *aff'd*, 327 F.2d 427 (7th Cir.); *cert. denied*, 377 U.S. 992; *rehearing denied*, 379 U.S. 872 (1964). Even though LaSalle did use terms such as "exceptional" and "most successful" when referring to the success of graduates featured in the testimonials, the net impression created was that such success was ordinary and typical of LaSalle graduates. The terms "exceptional" and "most successful" did not serve to mitigate nor to correct the false impressions created by the promotional materials.

Nor did subsequent qualifications in the brochures cure the initial deception of the advertisements. For example, in the computer programming brochure the text states:

> LaSalle can provide you with basic computer programming training. *If you combine this training with on-the-job experience,* you will discover what interesting work computer programming can be (CX 103C, 106C) (emphasis added).

Such a statement, indicating additional experience or training would be necessary to be a computer programmer trainee, is overshadowed by repeated representations that LaSalle's graduates would be qualified without further training or experience (Findings 146–47). Furthermore, the courts have found that when the initial contact with the consumer is procured by misrepresentation, as in LaSalle's advertisements, subsequent events or representations do not expunge the original [121]wrong. *Exposition Press Inc.* v. *FTC*, 295 F.2d 869, 873 (2nd Cir. 1961), *cert. denied*, 370 U.S. 917 (1962); *Carter Products* v. *FTC*, 186 F.2d 821, 824 (7th Cir. 1951).

In some instances, LaSalle's promotional materials contained conflicting or ambiguous statements about the anticipated level of entry of respondents' graduates in their career field (Findings 124, 126).[37] Ambiguous statements "susceptible of both a misleading and a truthful interpretation will be construed against the advertiser." *Murray Space Shoe Corporation* v. *FTC*, 304 F.2d 270, 272 (2nd Cir. 1962); *Rhodes Pharmacal Co.* v. *FTC*, 208 F.2d 382, 387 (7th Cir. 1953), *modified by restoring Commission's order in toto*, 348 U.S. 940 (1955).

LaSalle's advertisements, in the case of the interior decorating and air conditioning courses, represented that its graduates would be able to open their own businesses a career choice which implies an

[37] Consider, for example, the statement of objectives for the interior decorating course (see Finding 124). The statement that the course provides "basic knowledge" of various phases of interior decorating including procedures for establishing a decorating business is succeeded by the statement that upon completion graduates would be able "to apply sound decorating principles . . . to the complete design of one or more rooms in private homes or commercial establishments." The latter statement implies that the ordinary graduate will be able to function at an advanced level. Such a claim is ambiguous in light of the statement that the knowledge provided is "basic". In accordance with precedent, the ambiguity is to be resolved against respondents.

ability to perform at an advanced level in the chosen field without further training or supervision. In one advertisement, respondents equated LaSalle graduates with "trained beginners" and linked that term to "plenty of chances for a business of your own" (CX 5A).[38] To the extent that this and other representations were ambiguous, they are to be resolved against respondents. The claim had the capacity to create the impression that their graduates could function as fully qualified air conditioning service and installation men [122]without further training and supervision. Certain other representations concerning the ability of graduates to start their own businesses were essentially unambiguous.[39]

Finally, respondents typical interior decorating, computer programming, and air conditioning graduates were not qualified, without further training or supervision, to enter the job market at the levels represented in respondents' advertising and promotional materials (Findings 120–30, 155–71, 194–99). As a result such materials had the capacity to mislead.

Since respondents' typical graduates of the courses in question did not have the qualifications represented, the related earnings and employment representations for graduates in those fields of necessity also had the capacity to deceive (Findings 130–31, 170–71, 198–99).

B. Respondents Did Not Disclose Material Facts about the Cancellation and Refund Policy

Although no false facts are stated, the failure to disclose material information may cause advertisements or promotional [123]materials to be false and deceptive. *Simeon Management Corp.* v. *FTC*, 579 F.2d 1137, 1145 (9th Cir. 1978).

In the course of marketing their courses, respondents failed to adequately disclose the number of lesson assignments to be submit-

[38] Air Conditioning & Refrigeration
Field welcomes trained beginners. Good pay, good future—with plenty of chances for a business of your own (CX 5A).

[39] You can now train for a decorating career at home . . . You can prepare for a variety of positions leading to fine salaries—or plan to go into a profitable business for yourself . . . (CX 6B).

They turned their love for decorating into a dream career

* * * * * * *

I have formed my own company . . . also have an associate to work with me. We are doing offices, private homes and model home complexes (CX 9B).

Air Conditioning and Refrigeration

Big futures in air conditioning—with plenty of chances to start a business of your own! . . . (CX 4A).

ted in a course and the fact that lesson assignments were in some cases unevenly distributed throughout the course.[40] These were material facts necessary for the student to calculate his tuition obligation which was based on the number of lesson assignments he submitted for grading (Findings 200–28; see also pp. 144–45). The non-disclosure of these material facts combined with the confusion arising from LaSalle's inconsistent use of terminology had the tendency and capacity to mislead students about the nature and extent of their tuition obligation.

II. Restitution

Complaint counsel seeks restitution for graduates of LaSalle's computer programming, interior decorating, and air conditioning and refrigeration courses (CB 31). Respondents, citing *Heater* v. *FTC*, 503 F.2d 321 (9th Cir. 1974), assert that the Commission has no authority to order restitution in a Section 5 administrative proceeding; however, the Commission has not acquiesced in that decision. *Genesco, Inc.*, 89 F.T.C. 451, 478 (1977); *Lafayette United Corp.*, 86 F.T.C. 1093, 1095 (1975); *Holiday Magic, Inc.*, 85 F.T.C. 90 (1975). A restitution order in the administrative proceeding cannot be foreclosed on the basis of *Heater*.

Restitution is sought pursuant to the allegations of Paragraph 14 of the complaint. Those charges allege unfairness on the ground of respondents' failure to refund tuition when payment was induced by unfair and deceptive acts and where the courses were of little value in fulfilling the expectations raised by LaSalle's representations or contracts.

Different standards apply in determining when restitution is appropriate in the case of an administrative order to cease and [124] desist issued under Section 5 and when it is appropriate in the case of a proceeding under Section 19 of the FTC Act, in a Federal District Court. Section 19 is a consumer redress statute. In comparison, cease and desist orders of the Commission are intended to prevent illegal practices in the future not to exact compensatory damages for past acts. *FTC* v. *Ruberoid Co.*, 343 U.S. 470, 473 (1952). The Commission has ruled "that an [administrative] order directing restitutionary relief in such situations would not be for the purpose of redressing private injuries even though it may have the incidental effect of benefitting private individuals." *Curtis Publishing Co.*, 78 F.T.C. 1472, 1516 (1971).

[40] For example, if more than half of the lesson assignments to be submitted were included in the first volume of text, a student could become obligated for all the tuition at the end of that volume even though there were two additional volumes of text remaining in the course.

The critical question, in a Section 5 administrative proceeding seeking restitution, is the particular relief required to cure the unfair or deceptive acts documented in the individual case. It is necessary to "look beyond the challenged deceptive practices (they, after all, can be effectively remedied by proscribing specifically-described representations and by requiring affirmative disclosures)" to determine whether *retention* of funds obtained as a result of misrepresentation is in and of itself unfair. Where the retention of funds is unfair, restitution is the only appropriate remedy. *Credit Card Service Corp.,* 82 F.T.C. 191, 207 (1973); *Curtis Publishing Co.,* 78 F.T.C. at 1516.

A seller's retention of customer's funds has been defined as unfair "where the consumer, as a result of deception or fraud on the part of the seller, pays for a product or service but receives nothing of value in return or receives something that is either worthless or of only token value." *Universal Credit Acceptance Corp.,* 82 F.T.C. 570, 647-48, 650 (1973), *aff'd sub nom., Heater* v. *FTC,* 503 F.2d 321 (9th Cir. 1974) (reversed solely as to the authority of the Commission to order restitution);[41] *Curtis Publishing Co.,* 78 F.T.C. at 1516; *Credit Card Service Corp.,* 82 F.T.C. at 207-08.

In determining whether retention of funds is in and of itself unfair, two situations must be distinguished. The first is where the seller has exaggerated the value of a product or service which does have value, although its value is not as represented, *Credit Card Service,* 82 F.T.C. at 208. The second is where the disparity between the representations and the [125]ability of the product or service to fulfill those representations is so great that it has little or no worth for the purpose for which it was purchased, *Raymond Lee Organization, Inc.,* 92 F.T.C. 489, 631-37 (1978). *Credit Card Service,* in explaining the criteria of worthlessness, distinguished between products or services having no value and instances where value has been misrepresented.[42] In that case, restitution was denied where the protection given by a credit card service of $50 possible liability per card was considered of more than token value even though the service did not protect respondents' cardholders "from the crushing liability described by respondents." 82 F.T.C. 208.[43]

The criteria for a finding of worthlessness were further defined in *Raymond Lee Organization,* 92 F.T.C. 489 (1978). In that case, the

[41] It is clear, in view of the Commission's non-acquiescence in *Heater,* that the Commission still adheres to the principles enunciated in *Universal Credit Acceptance Corp. Genesco, Inc.,* 89 F.T.C. 451, 478 (1977); *Holiday Magic, Inc.,* 85 F.T.C. 90 (1975).

[42] ". . .demonstrating that the value of respondent's service is grossly exaggerated is not the same as showing that it is of no value." *Credit Card Service,* 82 F.T.C. at 208.

[43] In addition, the service resolved billing errors with credit card issuers and obtained new cards for persons whose cards had been lost or stolen. *Credit Card Service,* 82 F.T.C. at 208-09.

Commission for the first time expressly adopted what has been termed a relative standard of value. In accordance with that standard, the value of a product or service is not determined in a vacuum, but is decided relative to the claims made for it. Based on a relative standard, RLO, a patent and license promoting company, was found to offer a service of little or no worth. Not only did RLO generally fail to obtain patents or licenses thereby enabling customers to achieve the represented monetary rewards, they also failed to perform any service of value monetary or otherwise.

Therefore, if the sale of a product or service is secured by misrepresentation, retention of the purchase money is unfair where the product or service are worthless. However, where the product or service has more than token value, in relation to the claims made, the appropriate remedy is an order prohibiting the misrepresentations in issue as well as affirmative disclosure. *Raymond Lee Organization,* 92 F.T.C. at 631–37; *Credit Card Service,* 82 F.T.C. at 208–09.

The value of LaSalle's courses must be judged in light of the representations made about the courses. The question remains whether complaint counsel has met the burden of proof under the relative standard. [126]

The evidence concerning the value of respondents' courses consists primarily of surveys of LaSalle's students. In addition to the surveys, student testimony and expert opinion as to the value of the courses bears on any determination that the courses in question were of little or no worth.

At the heart of complaint counsel's case is a survey by the Research Planning Corporation (hereinafter designated as RPC) designed to measure the success of LaSalle's vocationally motivated graduates of the computer programming, interior decorating, and air conditioning and refrigeration courses.

The RPC survey of LaSalle graduates was designed essentially to measure the occupational success of those graduates whose vocational motivation prompted them to enroll in respondents' courses. In order to measure the success of LaSalle's vocationally motivated graduates, the RPC survey analyzed two areas. First, what motivated the students to take their course and how, if at all, LaSalle or its representatives influenced that motivation and second, what was the vocational and financial experience of the individuals taking such courses (CX 279C; Finding 259).

The results of the RPC survey were recomputed by Consulting Statisticians Inc. (hereinafter cited as CSI) on the basis of a narrow definition of success. Under this narrow definition, a vocationally

motivated LaSalle graduate, who responded that after graduation he obtained a new or better job or a higher salary, was considered successful if he also responded that the LaSalle course was instrumental in that achievement (Finding 281–87).[44]

Complaint counsel maintains that the success rate, as recomputed by CSI under the narrow definition, demonstrates that the three courses in question were of little or no value in fulfilling the course objectives which LaSalle had represented could be achieved on graduation. On that basis, complaint counsel contend that it was unfair for LaSalle to accept and fail to refund money obtained from students who were unable to accomplish the vocational goals which respondents had represented to be attainable by the ordinary and typical LaSalle graduate (CB 28–31). [127]

According to the survey results, as computed by CSI, 1.8 percent of all vocationally motivated LaSalle computer programming graduates not working in the field at the time of their enrollment had obtained a new or better job upon completion of the course and had indicated that the course helped them to do so. The comparable figure was 21.6 percent for interior decorating graduates and 13.2 percent for air conditioning graduates (Finding 287).

The aggregate figures for students achieving vocational objectives, including both those graduates working in the field and those not working in the field of the course at the time of enrollment, were substantially higher—8.9 percent in the case of computer programming, 24.6 percent in the case of interior decorating, and 23.1 percent in the case of air conditioning and refrigeration (CX 1081U, V, W)—than the figures based solely on those graduates who were not working in the field at the time of enrollment (Finding 287).

However, the threshold question is the validity of the survey. Respondents maintain that the RPC survey suffers from a number of defects in methodology which irreparably bias the results and, that because of such bias the survey should be given no weight. The RPC survey, in fact, suffered from a number of critical flaws.

One the most serious defects in the RPC survey instrument was the cover letter addressed to survey respondents. Under the letterhead of the "Federal Trade Commission, Chicago Regional Office," the letter began "The Bureau of Consumer Protection is gathering information from people who enrolled in LaSalle Extension University correspondence courses to determine if any action is warranted." The cover letter was signed by an individual identified as a Federal

[44] CSI also recomputed success rates under a broad and expectation based definition of success (Findings 283, 287). Since complaint counsel urges adoption of the narrow definition, the discussion will be confined to the recomputation under that definition.

Trade Commission attorney. In addition, the accompanying survey questionnaire was headed with the legend "Bureau of Consumer Protection Questionnaire, LaSalle Extension University Graduates" (Finding 293).

The cover letter introduced bias into the survey on a number of levels. Use of Federal Trade Commission stationery signaled that the survey was an inquiry under the auspices of the Federal government, references to the Bureau of Consumer Protection implied that LaSalle's students required protection, and statements in the letter that the survey was being conducted to determine if any action was warranted implied that LaSalle's conduct was questionable. As a whole, the letter suggested that LaSalle was under investigation for illegal practices injurious to the consumer (Finding 294).

As a general rule, covering letters for survey questionnaires should be as innocuous as possible so as not to bias those responding to the survey. The sponsor of a survey should not be noted where such indication could affect the [128]nature of the responses. The use of a cover letter and questionnaire indicating that the purpose of the RPC survey was a law enforcement investigation was not consistent with good survey practice (Findings 291, 297).

The cover letter created an atmosphere in which dissatisfied students would be more likely to respond than those who had had a positive experience with LaSalle. In general, persons with a grievance are more likely to respond to a mail survey. The effect of the cover letter was to induce self-selection by those graduates hostile to LaSalle (Findings 298–99).

The question of self-selection aside, the cover letter, by stating that LaSalle might be the subject of a law enforcement investigation and by implying wrong doing on the part of LaSalle by the fact of an FTC investigation, was likely to bias the responses to the survey questions in a manner adverse to LaSalle (Finding 300).

The effect of the bias inherent in the cover letter and the legend "Bureau of Consumer Protection" on the questionnaire was compounded by the fact that questions concerning subjective issues such as the students' motives in enrolling and their impressions of the representations made to them at the time of enrollment related, in a substantial number of cases, to events four or more years prior to the time of the survey (Finding 302).[45]

Certain key questions in the survey were phrased in a leading manner adverse to LaSalle (Finding 303). The effect of such leading

[45] Complaint counsel urges that the VA surveys also suffer by virtue of a time lag between the events surveyed and the survey itself. The critical difference is that the VA surveys were not subject to a number of sources of bias, as was the RPC survey, which compounded the problem of age.

questions was compounded by the biasing effect of the cover letter and the heading on the questionnaire (Finding 303).

In addition, the precoding (multiple choice answers) in certain questions in the survey instrument had the potential for introducing bias adverse to LaSalle (Findings 305–10). For example, in question 1, the narrow list of reasons provided for enrolling may have raised the percentage of vocationally oriented responses in a manner adverse to respondents. Since the number of vocationally oriented responses formed the denominator of the success ratio, the answers to question 1 materially affected the survey results (Finding 310). [129]

Questions 5–13 of the questionnaire excluded from success those students who got a new or better job in a field closely related to the field of training. These questions were adverse to LaSalle as they narrowed the number of responses classified as successful. In this connection, a salary increase attributed to a LaSalle course in a field closely related to the field of training would also be excluded (Finding 311).

Significantly, the RPC questionnaire did not ascertain or measure the degree of effort expended in seeking a job after graduation. The survey did not inquire about the number of interviews students obtained when seeking employment. Therefore, it is difficult to determine, on the basis of the RPC survey, how much credence to give to reasons of survey respondents for not getting a job after taking the course (Finding 315).

There is a tendency by survey respondents to check the first alternative in the case of multiple choice answers. The arrangement of precoded answers in some key questions so that the answer least favorable to LaSalle was placed first had the potential to bias the survey results. To avoid such bias, it would have been good practice to rotate the order of the precoded answers on the questionnaires (Finding 314).

The RPC survey questionnaire and the accompanying cover letter had the tendency to bias the survey results. Since surveys involve hearsay, proper safeguards must be observed to insure their reliability and accuracy when they are used as evidence. *Pittsburgh Press Club* v. *United States,* 579 F.2d 751, 758 (3d Cir. 1978). As the Seventh Circuit has noted in a Federal Trade Commission case, "the value of a survey depends upon the manner in which it was conducted—whether the techniques used were slanted or fair." *Rhodes Pharmacal Co.* v. *FTC,* 208 F.2d 322, 387 (7th Cir. 1953), *rev'd in part on other grounds,* 348 U.S. 940 (1955).

The factors to be considered in determining whether a poll or a

survey meets generally accepted survey principles may be summed up as follows:

. . .A proper universe must be examined and a *representative* sample must be chosen; the persons conducting the survey must be experts; the data must be properly gathered and accurately reported. It is essential that the sample design, the questionnaires and the manner of interviewing meet the standards of objective surveying and statistical techniques. Just as important, the survey must be conducted independently of the attorneys involved in the litigation. The interviewers or sample designers should, of course, be trained, and ideally should be unaware [130]of the purposes of the survey or the litigation. *A fortiori,* the *respondents* should be similarly unaware. . . . *Pittsburgh Press Club* v. *United States,* 579 F.2d at 758.

The cover letter which accompanied the RPC survey was rephrased in response to the Federal Trade Commission's request (Finding 292 and n. 23). Such action evidences involvement by the Commission in the manner in which the survey was conducted.

The danger of faulty memory on the part of survey respondents affects the weight to be given to a survey. In the case of some questions, particularly subjective questions, this is a greater danger than in the case of others. *Pittsburgh Press Club* v. *United States,* 579 F.2d at 758. In the instant case responses to subjective questions such as those concerning vocational motivation may have been affected by the number of years between the date of the student's enrollment and the date of the survey (Finding 302).

In addition, a survey may well be inadmissible or should be given no weight if the questions are "unfairly worded so as to suggest answers favorable to the party sponsoring the survey." In such a case, the required circumstantial guarantees of trustworthiness would be lacking, *Pittsburgh Press Club,* 579 F.2d at 758. Certain of the leading questions in the RPC survey and precoding of certain responses had the tendency to bias the survey results in a manner adverse to LaSalle (Findings 303, 305–10).

The RPC survey does not meet the requirements of circumstantial guarantees of trustworthiness, prerequisite to reliability. In addition to the above stated factors, the cover letter signaled the purpose of the survey and thus violated the principle that respondents should be unaware of the objective of the poll. That alone is sufficient reason to give the survey no weight.

The danger of informing respondents of the purpose of a survey in terms of self-selection as well as in terms of influencing the responses to the questions asked have been judicially summarized as follows:

. . .The respondents who were all club members and thus interested in the litigation, were told the precise nature of the litigation and the purpose of the survey. They consequently knew which responses would be helpful to PPC, and conversely which

would be harmful. Moreover, it was possible that a recipient of the questionnaire would fail to respond because he [131]knew an honest response would be harmful to the clubs position. Thus, respondents might have contained a higher percentage of those who could answer in a way helpful to the club. *Pittsburgh Press Club,* 579 F.2d at 759.

In this case, the cover letter alone, with its potential for multiple bias in the form of possible self-selection by respondents and with the additional potential for influencing the answers of those who did respond, requires that the survey be given no weight. Furthermore, the cover letter was likely to compound the effect of the leading questions in the survey as well as unduly influence those with a faulty memory concerning events preceding the survey, particularly where subjective questions were involved.

CSI computations made no effort to compensate for possible bias in the underlying data (Finding 282). The expert testimony that the survey suffered from inadmissible bias is persuasive. The fact that there was no statistical evidence concerning the effects of the potential bias is irrelevant. The proponent of survey evidence has the burden of establishing that it meets the requirement of circumstantial guarantees of trustworthiness. *Pittsburgh Press Club* v. *United States,* 579 F.2d at 758. In this instance, the burden has not been met. The survey is entitled to no weight.

Absent the RPC survey, the record evidence concerning the value of LaSalle's courses consists of expert and student testimony, and the surveys required by the Veterans Administration in 1975 and 1977.

Complaint counsel do not attack the methodology of the VA surveys as conducted by respondents (CRB 33). They contend, however, that these surveys are irrelevant for two reasons: first, the VA surveys do not ask respondents whether the LaSalle course contributed to a graduate's employment or a higher salary in the field of training (CRB 34); second, since the surveys do not segregate those graduates employed in the field at the time of enrollment and those who obtained employment in the field after graduation, the VA results do not support the contention that LaSalle graduates would be qualified without further training to obtain employment in the field (CRB 34).

The VA surveys do not focus specifically on the accuracy of respondents' representations. Accordingly, they are not relevant to the issue of misrepresentation. They are however germane to the restitution issue. The failure of the VA surveys to distinguish between those working in the field of training at the time of enrollment and those who only obtained employment after graduation does not preclude consideration of these surveys in connection

with the restitution issue. A course may [132]have value for students already in the field by making possible a promotion or a raise in pay. More importantly, absent the RPC survey (to which no weight has been given), the VA surveys provide the most comprehensive picture of vocational value available in the record. The VA surveys were mandated by Congress and are required by the VA pursuant to statute as a measure of vocational worth (Finding 322).[46] As such, the surveys were designed to give at least a rough measure of the vocational value of the courses. They should not be ignored in connection with the issue of whether respondents' courses were worthless or of token value.

The testimony of the Commission's experts established that the three courses in question would not qualify the ordinary and typical graduate, without further training, for entry into the fields of computer programming, interior decorating, and air conditioning at the levels represented in respondents' advertisements and promotional materials. However, the expert testimony did indicate that the courses were of some value in introducing the subject matter and teaching relevant principles at a basic level (Findings 349, 352, 354). The expert testimony also indicated that the courses may have some vocational value although the courses did not prepare the ordinary and typical graduate for the employment levels represented (Findings 351, 353, 355). The fact that the courses have some vocational value was corroborated by the testimony of respondents' graduate student witnesses who found the three courses helpful in their fields of training or related fields as well as by the statistics of the VA surveys (Findings 338, 342–43, 347). The findings on the extent to which the ordinary and typical graduate could benefit from the courses were based on the testimony of the experts. The extent to which the ordinary and typical graduate could benefit from the courses could not be determined on the basis of student testimony, absent a showing that such student witnesses were representative of the student populations of the three courses.

For the same reason, the student testimony could not support conclusive findings as to the influence of prior training or experience on the vocational success of LaSalle graduates. [133]

The relative value standard, as a prerequisite to restitution, is not self-defining. The degree of exaggeration at which a product or service becomes of little value, in the context of expectations arising from deception, must be defined on a case-by-case basis. However, it

[46] In one consent order pertaining to a correspondence school, the FTC required disclosure by respondents of VA survey figures *National Systems Corp., et al.*, 93 F.T.C. 58, 70 (1979). The fact that this provision may in the future be replaced by provisions of the TRR, 93 F.T.C. at 75 does not detract from the Commission's recognition of the VA surveys as a measure of vocational value.

is clear that restitution cannot be required in any case where mere exaggeration has been proven, a result the Commission disavowed in *Credit Card Service*, 82 F.T.C. at 208–09. To order restitution, there must be proof that the product or service claims so outstripped the actual value of the product or service that it was of little or no value for the purpose for which it was purchased.

The record indicates that the courses may have some vocational value. While the evidence is insufficient to rebut the finding that the qualifications of and demand for LaSalle graduates have been exaggerated to the point of misrepresentation, resolution of the restitution question requires an assessment of the evidence pertaining to vocational value in context of the representations made.

The question of little or no worth is necessarily intertwined with the subjective motivation of the students, the numbers that were in fact vocationally motivated, and of that group the number, if any, who achieved occupational success, and a measure of how close such success was to the expectations raised. Therefore, expert testimony or testimony from a limited number of students alone cannot be determinative as to whether the courses were of little or token value in fulfilling the expectations raised by respondents. Accordingly, survey or statistical evidence applicable to the populations enrolled in the three courses is required to resolve the issue of whether the courses were of little or no value. Absent such evidence, no finding can be made that restitution is the only effective remedy. The burden on this point has not been met by the government. The remedy should be limited to proscribing the misleading representations and requiring appropriate affirmative disclosure. Compare *Credit Card Service Corp.*, 82 F.T.C. at 207–09.

III. Remedy

A. Liability of Macmillan

The first question is whether Macmillan should be subjected to an order in this proceeding. Respondents urge that Macmillan is not responsible for the alleged law violations by its wholly-owned subsidiary LaSalle. They contend that LaSalle has at all times conducted its business as a separate corporation. Macmillan's relationship to LaSalle, respondents assert, was merely the incident of its ownership of LaSalle's stock and its [134]role as an investment banker attempting to manage financial assets (RB 78). In fact, the record demonstrates that Macmillan exercised more than incidental control over the affairs of LaSalle.

There has been extensive overlap between the officers and

directors of LaSalle and Macmillan (Finding 24). Macmillan executives received activity and financial reports from LaSalle (Findings 36–38). Macmillan reviewed and approved LaSalle's long range plans (Finding 39). Macmillan's approval was required for the following actions by LaSalle: the purchase of any capital asset costing more than $100; a significant revision in an existing course; funding for development of new courses; salaries for LaSalle personnel in excess of $20,000; the borrowing of money by LaSalle; expenditures for advertising in excess of budgeted amounts; personnel changes involving high-level LaSalle executives; and the execution of consent agreements with state or federal agencies when such agreements concerned LaSalle's operations. Macmillan's approval was required before LaSalle could discontinue marketing its courses through sales representatives and make a major investment in a mail order marketing program (Findings 43, 54).

Macmillan guaranteed the financial stability and performance of LaSalle to various accrediting agencies (Finding 44). LaSalle, when applying for accreditation renewal to NHSC, held itself out as a subsidiary of Macmillan and asserted the latter's financial support was its greatest asset (Finding 45). LaSalle participated in a common checking system established for its subsidiaries by Macmillan (Finding 48); Macmillan loaned money to LaSalle which did not have authority to borrow on its own behalf (Finding 49). Employees of Macmillan and LaSalle have participated in the same benefit programs such as a pension plan (Finding 50).

Macmillan's President sent a letter to the Indiana Private School Accrediting Commission conveying Macmillan's guarantee that LaSalle would furnish the educational services contracted. This assurance was ratified by Macmillan's Board of Directors (Finding 56).

Common law principles do not determine the liability of a parent company for the actions of its subsidiary in an enforcement proceeding under Section 5 of the FTC Act. Nor is complete control by the parent over the subsidiary so that the latter is "a mere tool and its corporate identity a mere fiction" prerequisite to piercing the corporate veil. *Beneficial Corp.*, 86 F.T.C. 119, 159 (1975), *aff'd in part and rev'd in part on other grounds*, 542 F.2d 611 (3d Cir. 1976), *cert. denied*, 430 U.S. 1983 (1977). *P.F. Collier & Son Corp.* v. *FTC*, 427 F.2d 261 (6th Cir. 1970), *cert. denied*, 400 U.S. 926 (1970); *Jim Walter Corp.*, 90 F.T.C. 671, 735 (1977). [135]

Ultimately the parent company's liability is to be determined on the basis of the "pattern and framework of the whole enterprise." *Art National Mfgs. Dist. Co.* v. *FTC*, 298 F.2d 476, 477 (2nd Cir. 1962),

cert. denied, 370 U.S. 939 (1962); *Providence Washington Insurance Co.*, 89 F.T.C. 345, 387 (1977); *Beneficial Corp.*, 86 F.T.C. at 159.

A parent corporation may be held for the acts of its subsidiary where the challenged conduct was performed directly by the subsidiary and where the parent corporation must be subject to vicarious liability or none at all. *Beneficial Corp.*, 86 F.T.C. at 159. Even, latent power to control the policy of its subsidiary is sufficient to hold the parent company vicariously responsible for the acts of its subsidiary *Beneficial Corporation*, 86 F.T.C. at 159.[47] If that standard is met, then there is no need to show that the parent company participated in or had knowledge of the challenged practices. See, *USLIFE Credit Corp.*, 91 F.T.C. 984, 1034 (1978).

The overall pattern of the interrelationship between Macmillan and LaSalle establishes Macmillan's vicarious liability for the acts of its subsidiary. *Providence Washington Insurance Company*, 89 F.T.C. at 387. The record shows that Macmillan reserved the right to control the business decisions of LaSalle and in a number of areas such control was actually exercised. At a minimum, the test of latent control has been satisifed, and Macmillan is subject to an order in this proceeding. [136]

B. Scope of the Order and Applicability of the Vocational Schools Trade Regulation Rule As Precedent

Complaint counsel propose an order requiring respondent to cease and desist from various misrepresentations primarily with respect to the qualifications of, demand for, and earnings potential of LaSalle graduates. In addition, complaint counsel propose provisions requiring extensive disclosure of the graduation, dropout, success and earning rates of LaSalle students and graduates, as well as of facts pertinent to students' financial obligations and cancellation of the courses. Respondents, who insist that no order is justified, have prepared a number of alternative provisions.

Certain provisions in the proposed order are patterned after the Commission's "Proprietary, Vocational and Home Study Schools" Trade Regulation Rule Trade Reg. Rep. ¶ 38,039 (1979) (hereinafter cited as TRR). The TRR is not presently in effect, *Katharine Gibbs School, Inc.* v. *FTC*, 1980–1 Trade Cases ¶ 63077, at 77348–49 (2nd Cir. 1979), rehearing denied March 17, 1980. Since the provisions of the

[47] [W]here a parent possesses latent power, through interlocking directorates, for example, to direct the policy of its subsidiary, where it knows of and tacitly approves the use by its subsidiary of deceptive practices in commerce, and where it fails to exercise its influence to curb illegal trade practices, active participation by it in the affairs of the subsidiary need not be proved to hold the parent vicariously responsible. Under these circumstances, complicity will be presumed. *P.F. Collier & Son Corp.* v. *FTC*, 427 F.2d 261, 270 (6th Cir.), *cert. denied*, 400 U.S. 926 (1970) cited in *Beneficial Corporation*, 86 F.T.C. at 159.

TRR are not controlling at this time, the question of remedy in this case must be confined to the record of this proceeding.

The purposes of rulemaking and adjudication are clearly distinguishable. Rulemaking, the Commission's legislative function, is appropriate where the objective is to establish standards by which an entire industry may be governed. Adjudication, by comparison, addresses itself to the factual and legal issues presented by the specific case. If the TRR is reinstituted, respondents will be bound by it as will other members of the industry.

The first question is the scope of the order. Respondents urge that the proposed order's coverage of "home study courses, home study training, self-study, self-improvement or other home study courses of instruction" is over broad (RRB 71–72). They contend that the term "self-study" could be construed as covering textbooks, Berlitz cassette language courses etc. (RRB 72). As respondents note, inclusion in the order of courses of this nature would cause difficult problems of construction. For example, do such courses have "graduates"? In addition, on the basis of this record, it would be difficult to determine whether it would be even possible to calculate placement data in the case of such courses. The provisions of the order directed to refunds would also be inapplicable.

Expenditures not reasonably related to or required for prevention of unfair acts and practices should not be imposed. *Katharine Gibbs School, Inc.*, 1980–1 Trade Cases at 77,349. The record in this instance contains sufficient information for a determination as to the impact of the order if its coverage is [137]broadened beyond home study correspondence courses. Under the circumstances, the order's coverage should be limited to home study correspondence courses, the subject of this proceeding.

C. Representations concerning Demand for, Qualifications of and Earnings Potential of LaSalle Graduates

Paragraph 1 of complaint counsel's proposed order is directed to misrepresentations concerning the demand for or earnings potential of LaSalle's graduates and their qualifications. These provisions are appropriate (See Findings 92–119, 132–54, 173–93) and will be adopted.

Directly related to the prohibitions against misrepresentations concerning demand for, qualifications of and earnings potential of respondents' graduates are the provisions of paragraph 2 directed to respondents' use of testimonials.

Respondents' use of testimonials implied that the experiences

portrayed were ordinary and typical of LaSalle graduates (Findings 95–105, 111–14, 140–43, 183–84, 193). Respondents should be permitted to make use of truthful testimonials, although the experience depicted was atypical, as long as the fact that such experience was not the ordinary is disclosed. *Raymond Lee Organization, Inc.*, 92 F.T.C. 489, 646 (1978).

The term "more successful" graduate does not dispel the overall impression that the testimonials were the ordinary and typical experience. An explicit disclosure that a testimonial is not the ordinary and typical experience will be required when that is the case. It is evident that the use of testimonials in advertisements devoted to a number of courses may be misleading, if the course taken by the endorser is not disclosed. A provision requiring such disclosure will also be adopted.

The proposed order would also require that the date testimonials were executed and the time period to which they apply be disclosed, that permission to use testimonials be obtained from the endorser every three months, and that the gifts or remuneration given to the endorsers be disclosed. The complaint does not allege that respondent's use of testimonials was misleading for the foregoing reasons and the evidence to support such provisions is at best minimal. In short, respondents were not put on notice either through the complaint or the manner in which the case was tried that these points were in issue and therefore did not have an adequate opportunity to defend with respect thereto. These provisions will not be adopted. [138]

Paragraph 3 of the proposed order would prohibit:

> 3. Failing to clearly and conspicuously disclose for any job or earnings representation made in any advertisement, the following disclaimer in print as large as the representation and in close proximity thereto:
>
> Graduation from this course does not mean you will get a job.

Respondents object to the required disclosure on the ground that it could be construed as meaning that "Graduation from this course means you will not get a job." They suggest as an alternative that the disclaimer read "Graduation does not guarantee that you will get a job" (RRB 73). Respondent's proposal appears adequate to prevent deception and will be adopted.

The order prohibits specific misrepresentations concerning the demand for, as well as the qualifications of and earnings potential of LaSalle graduates. In addition to prohibitions against specific misrepresentations, affirmative disclosures, may be required where it is necessary to prevent deception through what is implied or

omitted rather than by outright misstatements. *Raymond Lee Organization, Inc.*, 92 F.T.C. at 648; *Manco Watch Strap Co., Inc.*, 60 F.T.C. 495, 510 (1962). Respondents' advertising and promotional materials were pervaded by the success through LaSalle theme. The advertising and promotional claims relating to the demand for LaSalle graduates, their qualifications and earnings potential had the capacity to deceive by virtue of ambiguity, and the failure to state material facts. The placement rates and the earnings of LaSalle graduates were material to the decision to enroll in light of such advertising and promotional claims. The order will accordingly require disclosure of the placement rates and earnings of LaSalle graduates from courses in connection with which employment demand and earnings representations are made.

The provisions in complaint counsel's proposed order requiring disclosure of placement and earnings rates are patterned after the disclosure requirement of the TRR. Complaint counsel urge that the proposal meets the Second Circuit's criticism in *Katharine Gibbs*, 1980-1 Trade Cases ¶ 630,077, of the Rule's requirement for placement disclosure; the proposed order, to meet those objections, permits respondents to disclose the number of graduates who could not be contacted, did not respond to inquiries or did not seek jobs within six months of graduation and the reasons why such individuals did not look for jobs (CB 15-16). [139]

Complaint counsel propose the following base period for calculating placement, earnings, dropout and graduation statistics for purposes of disclosure under the order:

> The First Base Period shall be the two (2) year period ending three (3) months prior to the effective date of this Order. Subsequent base periods shall be of two (2) year duration commencing on the next day following the termination of the prior base period. Base periods shall be numbered consecutively beginning with the first base period (*i.e.*, Base Period #1) as defined above.
>
> The three (3) month period immediately following the close of a base period shall be used by respondents to record and compile the information required by Part I, Paragraph 4 and Appendix A. In addition, respondents may not include in the computation of students for the base period any person whose enrollment terminated during the three (3) month recordation period. Such persons will be included in the statistics for the subsequent base period (Appendix B, Proposed Order).

Job placements and earnings within six months of graduation are to be recorded under the provisions of the proposed order (Appendix A, Proposed Order). Complaint counsel urges that the record supports the use of placement figures based on a six month period because testimony from vocationally motivated graduates demonstrates they sought employment within that time (CB 16).

Respondents object to complaint counsel's disclosure provisions on a number of grounds (RRB 76, *et seq.*). They first object that such disclosure should be required only when LaSalle represents there is an employment demand for the graduates of a particular course. This objection is valid. Requiring disclosure of this nature will impose requirements that LaSalle graduates be surveyed and necessitate extensive record keeping requirements in connection therewith. Under the circumstances, such a requirement should only be imposed in the case of those courses where vocational claims are made.

A number of other objections to complaint counsel's proposal concerning placement rate disclosure are pertinent: those who make no or only an inadequate effort to find employment should [140]not be counted as failures, and placement success should include not only jobs in the field of the course, but also those in a closely related field requiring substantial use of the skills learned in the course. Respondents also claim that the proposed base period for placement rates would understate LaSalle's success in this area. The proposed base period covers employment obtained within six months after graduation. However, such data is to be obtained by a survey within the three months succeeding the conclusion of the base period. As a result, those graduating at the end of the base period who did not obtain almost immediate employment would not be counted and respondent would be disadvantaged at least on the basis of the calculations for the first base period. Respondents' proposal designed to minimize such problems will be adopted.

The decision to require disclosure of the graduates' placement and earnings rates as facts material to the decision to enroll obviates the need for additional provisions in the order to assure the advertisements have a reasonable basis. Accordingly, no findings with respect to the issue of reasonable basis for respondents' advertisements are made.

D. The Selectivity Allegations

1. Representations That Students Were Screened To Determine Whether They Would Benefit from the Course

Respondents represented that LaSalle was open to qualified students (Findings 238–39), and sales representatives were instructed that the "qualifying interview" was the heart and core of the standard sales presentation. This technique, according to respondents, put the burden on the prospective student to tell the LaSalle representative why he was qualified (Finding 240).

Respondents' advertising and promotional claims as well as the sales presentation had the tendency and capacity to create the impression that, over and above the standard minimum age and educational requirements generally applicable, respondents were selective in enrolling students. They created the impression that students had been screened to determine that the students would benefit from particular courses. Such representations were false or misleading since respondents' students were not screened for the specific aptitudes helpful to successful completion or assimilation of particular courses (Findings 244–49, 256–58). [141]

A school's misrepresentation of its selectivity in accepting prospective students is deceptive and unfair within the meaning of Section 5 of the Federal Trade Commission Act. *Arthur Murray Studio of Washington Inc.*, 78 F.T.C. 401, 440 (1971), *aff'd*, 458 F.2d 622 (5th Cir. 1972); *Tractor Training Service*, 50 F.T.C. 762, 769, 776 (1954), *aff'd*, 227 F.2d 420 (9th Cir. 1955), *cert. denied*, 350 U.S. 1005 (1956). Respondents' representations that they screened prospective students to be sure they were "right" for or would benefit from a course (Finding 251) support imposition of a requirement that graduation and dropout rates be disclosed. In the light of such representations, the dropout and graduation rates are material factors for the prospective student in his enrollment decision. This data will facilitate the evaluation of claims that LaSalle's students are screened prior to acceptance.

Disclosure of dropout and graduation rates will be required for the three calendar years preceding contact with the prospective student. The requirement is not burdensome. Such information is already in respondents' files. A three year period is adopted to meet the objection that the base period selected by complaint counsel would unduly overstate dropout and understate graduation rates.

2. Negative Sell

Respondents' sales representatives were instructed that the Confidential Qualifications Questionnaire was a powerful sales tool for someone "who has learned to use it for all it's worth" and that it could be used to meet objections and stalls by prospective students when the time came to close the sale (CX 153 O). LaSalle's sales representatives were instructed to use the Qualifications Questionnaire to elicit information helpful in making a sale such as the prospect's "inner feelings" and "his hopes and feelings about his future" (CX 153M–N). LaSalle's sales representatives, in the case of the "complacent" prospect, were instructed to create dissatisfaction with respect to present earnings and to "help him identify his inner

discontent." In the case of an already dissatisfied prospect, sales representatives were to "encourage him to give you the details" (CX 153BB–CC). The LaSalle representations concerning demand for and earnings potential of its graduates (Findings 93–108, 133–45, 173–85) held out LaSalle as the answer to such feelings of dissatisfaction.

Paragraph 11 of the complaint alleges that respondents have unfairly disparaged the present or potential career opportunities, training, education or other personal characteristics of prospective students, and represented [142]directly or indirectly that respondents' correspondence courses could alter such characterics for the better.

This technique is referred to by complaint counsel as the "negative sell". According to Commission counsel, the negative sell is a more egregious form of the selectivity representations by virtue of the emphasis on creating "dissatisfaction in the prospective student and the offering of LaSalle as the salvation for that discontent" (CB 20).

The relationship of the negative sell to the selectivity misrepresentations is not readily apparent. Complaint counsel urge that subtle manipulation of the Qualifications Questionnaire was used to stimulate the prospect's discontent and thus make him more amenable to the sales pitch for LaSalle as the hope for improvement (CB 20). They argue further that after feelings of dissatisfaction have been created, the prospect becomes more vulnerable to that part of the sales presentation designed to convince him that he must persuade the sales representative that he should be allowed to enroll.[48] It would be equally logical to link the charges under Paragraph 11 of the complaint to the allegations concerning misrepresentation of demand for and earnings potential of LaSalle graduates.

Creating discontent or dissatisfaction in order to stimulate the sale of a product or service is not *per se* unfair. However, it may become unfair when it results from deception or other unfair practices. Here, sales representatives were instructed to arouse discontent in the course of a sales presentation designed to give the overall impression that prospective students had to prove they were qualified to take the course. At the heart of that procedure was the Qualifications Questionnaire which salesmen were told was a sales tool which [143]

[48] Complaint counsel argue:

The prospective LaSalle student, a victim of these artificially created feelings of dejection and dissatisfaction and a potential recipient of the benefits that can be achieved from LaSalle, feels more compelled, than if LaSalle had only misrepresented its selectivity, to convince the sales representative to allow him to enroll in a LaSalle course and thereby increase his earnings, train for a new or better career and thereby gain admission to a new and better life (CB 20).

they should use "for all it's worth." There is an element of unfairness here.

Practices such as the negative sell technique present difficult problems in fashioning a remedy. Prohibitions designed to prohibit practices such as undue sales pressure are apt either to be so narrowly drawn as to be ineffective or so overbroad as to be unenforceable. *Arthur Murray*, 78 F.T.C. 401, 441 (1971); *aff'd*, 458 F.2d 622 (5th Cir. 1972).

The requirement, entered in response to the general selectivity allegation, that respondents disclose dropout and graduation rates will enable prospective students to evaluate respondents' claims, if any, with respect to selectivity. There does not seem to be an additional need for rejection rates to afford a further basis of evaluation. The provisions of the order, entered pursuant to other charges, requiring disclosure of placement and earnings rates and prohibiting misrepresentations with respect to demand for, earnings potential and qualifications of LaSalle graduates should also effectively preclude the violations alleged under Paragraph 11 which were the result of the negative sell technique. No additional provision is required.

3. Contract Terminology

Paragraphs 11, 12, and 13 of the proposed order would prohibit representations that a contract for sale is anything other than a retail installment contract, prohibit the use of such terms as "Applicant's Copy" on an enrollment contract, and require that the student's copy of a contract be labeled "Purchaser's Copy". Complaint counsel urge that these provisions are designed to prohibit use of terminology with the tendency and capacity to create the impression that LaSalle was selective in enrolling applicants (CB 22).

The bulk of the contracts received as evidence in this proceeding and in use during the relevant period do not give the overall impression that they are "applications" rather than retail installment contracts. Most are labelled "retail installments contracts" and the overall appearance of these documents indicate that they are in fact contracts and binding upon the prospect if accepted *(e.g.*, CX 200).

The provisions of Paragraphs 11, 12, and 13 will not be adopted. The violations with respect to misrepresentation of selectivity can be adequately remedied by requiring disclosure of dropout and graduation rates, as well as requiring respondents to cease and desist from representing that prospective students are screened for aptitudes

helpful in assimilating the subject matter of specific courses unless such is the fact. [144]

The provisions proposed in paragraphs 11–13 appear more germane to an allegation that respondents misrepresented the nature of their contracts or that students were misled into believing the transactions were not sales. In *Eastern Detective Academy*, 78 F.T.C. 1428, 1465, 1471 (1971), on which complaint counsel rely in connection with this point, there was an express allegation that the nature of the instruments had been falsely represented. Such charges are not contained in this complaint,[49] therefore, the suggested provisions are not justified.

E. Failure To Disclose Material Facts in Connection with the Student's Financial Obligation

Since 1973 LaSalle's refunds to students withdrawing from or cancelling a course were based on a percentage calculated from the number of lesson assignments submitted for grading over the total number of lesson assignments in the course (Finding 204).[50] Under the quartile tuition policy the number of [145]lesson assignments to be submitted in a course was therefore a material fact which the student needed to know to calculate his tuition obligation at any point in the course.

In many of LaSalle's courses, the lesson assignments to be submitted for grading were not distributed evenly throughout the course in relation to the text to be covered (Finding 201). In many courses, the greater number of lesson assignments on which the tuition obligation depended were placed at the beginning of the course, a practice known as front-end loading (Finding 200–01).

LaSalle's contracts, which generally stated the applicable refund policy, prior to 1979 did not, with some exceptions, state the total number of lesson assignments to be submitted in the given course. Other LaSalle materials, such as the course brochure, which did give

[49] Some of the contracts labeled "Retail Installment Contracts" had a space for "applicants" signature on the Enrollment and Credit Information page which was an application for credit *(e.g.*, CX 199B). The contracts themselves had a space for "buyers signature" *(e.g.*, CX 199A). One salesman testified that he referred to the contracts as "agreements" because it sounded "softer" (Wilmot 817).

If the complaint contained the appropriate allegations, RX 851 and 852 entitled "Enrollment Application and Agreement," which were in fact retail installment contracts, might justify an order prohibiting misrepresentations as to the nature or significance of **respondents'** installment contracts. These, it may be noted, are mail order contracts and would not have been used in connection with a representative's sales presentation or the Qualifications Questionnaire.

[50] In most instances, the following tuition refund policy applied: a student owed a registration fee plus 25 percent of the total tuition obligation if he submitted less than 25 percent of the lesson assignments to LaSalle for review; 50 percent of the tuition was owed if the student submitted more than 25 percent but less than 50 percent of the lesson assignments and the total tuition was owed when the student submitted more than 50 percent of the lesson assignments (Finding 205).

such information did not state the cancellation or refund policy and frequently used terms for lesson assignments inconsistent with the terminology in the contract. Finally, neither the enrollment contract or other materials furnished to students before enrollment advised prospective students that readings between lesson assignments increased as the course progressed (Findings 200–03, 214–20).

The record demonstrates that the interaction of the front-end loading of LaSalle's courses with the quartile refund policy confused respondents' students as to their financial obligations and their right to a refund on cancellation or withdrawal from the course (Finding 227). The failure to clearly disclose the number of lesson assignments in the particular course constituted the failure to disclose a material fact. The practices of front-end loading and inconsistent use of contract terms coupled with the failure to disclose material facts had the tendency to mislead and was unfair.

The confusion arising out of the interaction of respondents' quartile tuition policy and front-end loading justifies a general prohibition against misrepresenting in any manner a student's financial obligations or failure to disclose material facts concerning his tuition obligations or right to a refund. A provision prohibiting respondents from failing to make the correct refund payment is also needed to prevent future unfair practices related to violations shown.

In addition, consumers must be furnished the following information: [146]

1. That their tuition obligation is based upon the percentage of the lesson assignments which they have submitted to LaSalle, compared to the total number in the course;
2. That a lesson assignment means those examinations, assignments, projects, etc., which they are required to submit to LaSalle for grading or evaluation;
3. The total number of lesson assignments in the course;
4. The lesson assignment which mark the various increments in the tuition obligation and the amount of tuition owed at each point; and
5. Detailed instructions to cancel the contract and how to apply for a refund including all conditions pertinent thereto.

To preclude further confusion respondents will be required to use only the term "lesson assignment" to refer to lesson assignments to be submitted to LaSalle and to use the term "lesson assignment" consistently in all their contracts, advertisements and promotional materials.

With this information in hand, the consumer can calculate his tuition obligation and his right to a refund at any point in the course. No further information is needed. The extensive data as to the structure of the LaSalle courses such as number of volumes of text, etc. required by paragraphs 5 and 9 of the proposed order is unnecessary. Nor would a requirement that all course materials be mailed at once serve any significant remedial function.

Paragraph 8 of the proposed order would in effect require respondent to abandon the quartile tuition policy and adopt pro rata refunds. This provision will not be adopted. The quartile tuition policy, as such is not inherently unfair. To the extent that respondent's refund and cancellation policies were unfair in practice, those violations will be cured by the disclosure requirements of the order to be issued herein.

F. Cooling Off Period

Complaint counsel assert, in support of their argument for a 14-day cooling-off period, that their proposed affirmative [147]disclosure requirements, necessitate that the consumer be given additional time for reflection (CB 18). There is insufficient evidence in this proceeding to support a finding that consumers have too little time to consider their purchase. Under LaSalle's contracts, in effect in the relevant period, consumers had six days to cancel without penalty or obligation *(e.g.*, CX 200E, 201E). There is no showing on the basis of this record that six days was insufficient time for reflection. If the period is to be extended, as a matter of policy, to 14 days, it should be done in the context of an industry wide rulemaking proceeding.

Conclusions

1. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and over the respondents.

2. The complaint herein states a cause of action and the proceeding is in the public interest.

3. The aforesaid acts and practices of the respondents as found in the foregoing Findings of Fact were and are to the prejudice and injury of the public and constituted, and now constitute, unfair and deceptive acts and practices in commerce in violation of Section 5 of the Federal Trade Commission Act. [148]

ORDER

I.

It is ordered, That respondents Macmillan, Inc., a corporation, and LaSalle Extension University, a corporation, their successors and assigns and their agents, and respondents' agents, representatives and employees, directly or through any corporation, subsidiary, division, franchise or other device in connection with the advertising, promoting, offering for sale, sale or distribution of home study correspondence courses, in any subject, field, trade or vocation in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended, do forthwith cease and desist from:

1. Misrepresenting, orally, visually, in writing or in any other manner, directly or by implication:

(a) The need or demand for persons completing any of respondents' courses or otherwise misrepresenting the opportunities for employment, or opportunities of any other type, which are available to such persons, or that persons completing said courses will or may earn a specified amount of money, or otherwise misrepresenting by any means the prospective earnings of such persons;

(b) The employment prospects of respondents' graduates or the ease with which respondents' graduates will be able to obtain employment;

(c) The type of jobs available to respondents' graduates, or that there will be job security or steady employment for respondents' graduates in positions for which respondents train such persons;

(d) The qualifications or requirements necessary to obtain employment in the fields for which respondents offer correspondence training, [149]including whether experience or additional education is required or advantageous for employment in any field or for any position;

(e) The types of jobs for which respondents' graduates will be qualified upon completion of respondents' courses;

(f) A student's financial obligations upon enrollment or failing to disclose material facts concerning a students right to cancel, his tuition obligations, or right to a refund.

2. The use of testimonials in any advertisements unless:

(a) the testimonial reflects the experience of the typical and ordinary LaSalle student; *provided, however*, that if the testimonial does not reflect the typical or ordinary experience of a LaSalle

student, a disclaimer stating that "this testimonial does not reflect the typical or ordinary experience of LaSalle students" shall be displayed in print as large as that of the testimonial itself, adjacent to or integrated with the testimonial;

(b) The testimonial states the LaSalle course or courses from which the endorser graduated and upon which his/her alleged success is based.

3. Failing to clearly and conspicuously disclose for any job or earnings representation made in any advertisement, the following disclaimer in print as large as the representation and in close proximity thereto:

Graduation from this course does not guarantee you will get a job. [150]

4. Failing to provide to any prospective enrollee prior to the signing of any contract or other agreement for enrollment in any course of instruction offered by respondents, a written disclosure form in 10 point bold face type containing the following information, under the heading "Notice to Prospective Students" with appropriate subheadings in 16 point boldface type, the information required by paragraphs II–1 through II–7 of this order.

5. Failing to disclose, in close proximity to the cancellation and refund clause in respondents' contracts, the information required by paragraph II–7 of this order.

6. Failing to provide the student with the correct refund payment, if any, or to cancel that portion of the student's indebtedness that exceeds the amount due the school and return any negotiable instrument executed by the prospective student in connection with the contract or sale within twenty-one (21) days of the receipt of notice of cancellation from the student.

7. Representing in any manner that prospective students are screened for the aptitudes helpful in or necessary to assimilating the subject matter of specific courses, unless such is the fact.

II.

It is further ordered, That:

1. If respondents represent to any prospective student of a LaSalle course that there is an employment demand for graduates of that course, LaSalle shall clearly and conspicuously disclose to such

prospective student the vocational success rate of graduates of that course defined by the following fraction (expressed as a percentage):

Numerator

Those graduates who obtained jobs or self-employment in the field of their [151]correspondence course or in a closely related field,[51] plus those graduates whom the course helped to obtain a promotion or earnings increase.

Denominator

All graduates who took the course in order to obtain new or improved jobs or to increase their earnings, less those who have not worked in the field of their course or in a related field, and who have not made a serious effort to find such a position.

A serious effort to find such a position shall be defined as interviewing three or more potential employers in the field of the course or a related field, or being advised by reliable sources that such efforts would be futile.

Such data shall be collected at least once every two years by a statistically valid survey of all LaSalle graduates who graduated within a period which is not less than twelve months, and which begins not more than three years before the questioning of graduates in each survey. Data obtained from any such survey shall not be published to prospective students more than twenty-four (24) months after the commencement of such survey questioning.

Such disclosure shall be made before the prospective student signs any enrollment application or agreement or otherwise commits himself to enrollment with LaSalle.

2. If respondents make representations to prospective students of a LaSalle course concerning the earnings potential of graduates of that course, they shall disclose the following information collected by a statistically valid survey conducted pursuant to the provisions of Paragraph II–1 of this order:

(a) on the basis of gross yearly earnings, the percentage of graduates in each [152]income bracket broken down by $2,000 increments, *e.g.*,

$4,000 - 6,000 — 30%

[51] For the purposes of this order, a closely related field means one which requires substantial usage of the skills learned in the course.

(b) the number and percentage of graduates who refused to provide salary information.

3. In connection with the disclosure of the vocational success rate or earnings rate required by Paragraphs II–1 and II–2 of this order, respondents shall also disclose the total number of graduates of the course in the period covered by the survey, the sample size of the survey, and the total number of responses received to the survey.

4. If respondents make claims as to the demand for and earnings potential of LaSalle graduates within the scope of Paragraphs II–1 and II–2 concerning a new course whose duration did not trigger the surveys required by these paragraphs then respondents shall clearly and conspicuously disclose that fact as follows:

THIS COURSE HAS NOT BEEN IN OPERATION LONG ENOUGH TO INDICATE WHAT, IF ANY, ACTUAL EMPLOYMENT OR SALARY MAY RESULT UPON GRADUATION FROM THIS COURSE.

5. If respondents make claims that they screen students for admission or that they are selective in enrolling prospective students for any course they shall disclose the dropout and graduation rates of students enrolled in that course for the three calendar years immediately preceding contact with the prospective student. Such disclosure shall specify the years to which such disclosure pertains.

6. In the case of a new course where respondents do not have the data required by Paragraphs II–5, they shall disclose dropout and graduation rates for those calendar years for which such data is available. If no dropout or graduation rate data is available for any calendar year that fact is to be disclosed.

7. If respondents utilize a quartile refund policy as defined by Findings 204–05 herein or a similar policy or plan, they shall disclose the following information to prospective students in the contract in close proximity to the cancellation and refund clause (This information is to be included both in the contract and in the "Notice to Prospective Students"): [153]

1. That their tuition obligation is based upon the percentage of the lesson assignments which they have submitted to LaSalle, compared to the total number in the course;

2. That a lesson assignment means those examinations, assignments, projects, etc., which they are required to submit to LaSalle for grading or evaluation;

3. The total number of lesson assignments in the course;

4. The lesson assignments which mark the various increments in

the tuition obligation and the amount of tuition owed at each point; and

5. Detailed instructions to cancel the contract and how to apply for a refund including all conditions pertinent thereto.

III.

It is further ordered, That "lesson assignment(s)" is the only term which may be used to refer to lesson assignments to be submitted to LaSalle and that the term "lesson assignment" must be used consistently in respondents' contracts, advertising and promotional materials. All respondents' contracts and "Notices to Prospective Students" must contain the following clause:

Lesson assignments are examinations and other exercises which are submitted to the school for grading; they do not include self-tests. The amounts of reading and other work for different lesson assignments vary in length, and generally become longer as the course progresses.

IV.

It is further ordered, That respondents maintain for a period of three (3) years, records which shall show the manner and form of respondents' continuing compliance with the above terms and provisions of this order. [154]

V.

It is further ordered, That respondents notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondents such as dissolution, assignment, or sale resulting in the emergence of a successor corporation or corporations, the creation or dissolution of subsidiaries or any other change in the corporations which may affect compliance obligations arising out of the order; *provided, however,* that if respondents do not have thirty (30) days lead time between the proposal of such change and its consummation, respondents shall notify the Commission thereof at the earliest feasible time before consummation and any entity which may succeed to any part of the business covered by this order will have been advised of every provision of this order and will have agreed to be bound thereby.

VI.

It is further ordered, That the respondents herein shall within

sixty (60) days after service upon them of this order, file with the Commission a report, in writing, setting forth in detail the manner and form in which they have complied with this order.

VII.

It is further ordered, That nothing herein shall relieve respondents from compliance with a Trade Regulation Rule, governing the advertising or promotion of educational courses of instruction subject to this order, in the event such a rule becomes final. [155]

Appendix A

Ans. Par. – Paragraph of the Answer
CB – Complaint Counsel's Brief
CRB – Complaint Counsel's Reply Brief
CX – Complaint Counsel's Exhibit
Comp. Par. – Paragraph of the Complaint
RA – Respondents' Admissions
RB – Respondents' Brief
RRB – Respondents' Reply Brief
RX – Respondents' Exhibit

Final Order

On June 12, 1980 the Commission stayed the effective date of the unappealed Initial Decision in this matter, pending a determination whether or not the matter should be docketed for review. After further consideration, the Commission has decided not to place the case on its docket, but instead to lift the stay and allow the Initial Decision to become the decision of the Commission.

It is hereby ordered, That the Initial Decision become the decision of the Commission, and that the order to cease and desist be entered.

IN THE MATTER OF

GROLIER, INCORPORATED, ET AL.

Docket 8879. Interlocutory Order, Sept. 12, 1980

ORDER REOPENING PROCEEDING AND DIRECTING SUBMISSION OF FURTHER INFORMATION

On January 24, 1980, the United States Court of Appeals for the Ninth Circuit remanded this case to the Commission.[1] *Grolier, Inc.* v. *FTC,* 615 F.2d 1215, 1222 (9th Cir. 1980). The purpose of the remand was to allow us to reconsider our denial of discovery "and in light of the results of that reconsideration, the disqualification motion" filed by Grolier. 615 F.2d at 1222. The Court did not require us to grant discovery but instead authorized the use of affidavits to show "the existence and extent of ALJ von Brand's involvement with the Grolier case while he served as attorney-advisor." *Id.* Under the procedure established by the Court, Grolier then has the burden of offering evidence to contradict these sworn statements or show any deficiency in them before it will be permitted to subpoena agency records. *Id.*

The Court mandated this course of action to us because it believed that our order denying discovery (87 F.T.C. 179, 181 (1976)) was an improper "flat refusal" (615 F.2d at 1222) to disclose anything at all about Judge von Brand's participation in the Grolier case while he was an attorney-advisor to Commissioner MacIntyre.

Since we denied the combined disqualification and discovery motion, however, Grolier has gained access to most of the information sought in its discovery request by virtue of a Freedom of Information Act ("FOIA") request that repeated the discovery request *in haec verba.* Indeed, most of the documents sought and an index of the few documents withheld have been available to Grolier since before Judge von Brand issued his Initial Decision. We note that the record of the district court proceeding contains much information, in affidavit form, which may make the discovery request moot. *Grolier, Inc.* v. *FTC,* No. 76-1559 (D.D.C.), *appeal pending,* D.C. Cir. No. 79-2263. We invite the parties to address this issue in the filings required by this order.

Because our earlier view was that attorney-advisors do not perform investigative or prosecutive functions there was no need for us to determine which of the twenty documents Grolier appended to the disqualification motion actually reached the Commission or

[1] A petition for rehearing was denied but the opinion was amended on April 17, 1980.

whether they involved this "or a factually related case." See 5 U.S.C. 554(d). The need for this type of analysis is apparent in view of the Ninth Circuit's ruling. We believe the parties should address these questions in their submissions.[2]

A related concern is what effect, if any, Grolier's failure to use documents in its possession before the Initial Decision issued should have on its ability to augment the record now. Some courts have held that the failure of a party to use information in its possession (from whatever source) renders a belated disqualification challenge untimely. See, *e.g.*, *Marquette Mfg. Co.* v. *FTC*, 147 F.2d 589, 592 (7th Cir. 1945), *aff'd.*, 333 U.S. 683 (1978); *Safeway Stores, Inc.* v. *FTC*, 336 F.2d 795, 802 (9th Cir. 1966), *cert. denied*, 386 U.S. 932 (1967). See also *Marcus* v. *Director, Office of Wkrs' Comp. Prog.*, 548 F.2d 1044, 1050–57 (D.C. Cir. 1976). We urge the parties to address this issue also.

To provide a complete record on review and to minimize delay Grolier is directed to supplement the record of this proceeding, within five days of the receipt of this order, with: (1) the complaint (and attachments) filed in its FOIA suit *Grolier, Inc.* v. *FTC*, C.A. No. 76–1559 (D.D.C.); (2) the affidavit and index of documents filed by the Commission in response thereto; (3) the Commission's sworn answer to Plaintiffs' Interrogatories to Defendants—Second Set; (4) the affidavit of Carol M. Thomas dated September 15, 1977; (5) all memoranda, orders and judgments of the District Court in No. 76–1559 (D.D.C.); and (6) the affidavit of Carol M. Thomas dated March 21, 1979.

Thereafter Grolier will be allowed 25 days to renew its motion to disqualify Judge von Brand. At that time we expect Grolier to present evidence on: (1) the question of timeliness; (2) Judge von Brand's involvement with *ex parte* matters; (3) the specific documents, and the portions thereof (and the date Grolier received them), which show Judge von Brand could have had access to "information received outside of the controlled adjudicative setting" (615 F.2d at

[2] The Attorney General's Manual on the Administrative Procedure Act (1947), characterized by the Court of Appeals (615 F.2d at 1219) as an authoritative guide to the APA states (p. 54, n.6):

> The limitation of the prohibition against consultation to those who perform investigative or prosecuting functions "in that or a factually related case", should be construed literally. * * *
>
> * * * * * * *
>
> The phrase "factually related case" connotes a situation in which a party is faced with two different proceedings arising out of the same or a connected set of facts * * * [as distinguished from cases that] may form a pattern similar to those which [the staff person] had theretofore investigated or prosecuted.

See also *Cisternas-Estay* v. *INS*, 531 F.2d 155, 161 n.4 (3d Cir.) (Gibbons, J., dissenting), *cert. denied*, 429 U.S. 853 (1976).

1220); and (4) whether the information involves this or a factually related case.

We also direct complaint counsel to review the 28 documents withheld from Grolier in the FOIA suit and ascertain what connection, if any, they have to the facts of this case. The results of this review shall be set forth in an affidavit to be filed and served (by express mail) within 15 days of this order.

Within a like period we request that Judge von Brand execute an affidavit recording his efforts to ascertain the extent, if any, of his involvement with Grolier matters while he was an attorney-advisor. The Secretary shall expeditiously serve the affidavit on the parties.

Complaint counsel may respond to Grolier's renewed motion within 20 days of being served with it. At that time the Commission will determine if any further proceedings are warranted.

Commissioner Pitofsky did not participate.

In the Matter of

totes incorporated

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-3040. Complaint, Sept. 12, 1980—Decision, Sept. 12, 1980

This consent order requires, among other things, a Loveland, Ohio manufacturer of umbrellas and related rainwear, to cease withholding cooperative advertising credits or allowances, or in any way limiting or restricting dealers from participating in any cooperative advertising program because of the resale price at which the dealer has advertised or sold a product or because the dealer has used price comparisons in the advertising and sale of a product.

Appearances

For the Commission: *Jeffrey A. Klurfeld.*

For the respondent: *William Baskett* and *Foston Jacobs,* Cincinnati, Ohio.

Complaint

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that totes incorporated, a corporation, hereinafter sometimes referred to as respondent, has violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges as follows:

For purposes of this complaint, the following definitions shall apply:

"Product" is defined as any item which is manufactured, offered for sale or sold by respondent.

"Dealer" is defined as any person, partnership, corporation or firm which is authorized by respondent to purchase any product.

"Resale Price" is defined as any price, price floor, price ceiling, price range, or any mark-up, formula or margin of profit used by any dealer for pricing any product. Such term includes, but is not limited to, any retail price suggested or established by respondent, any customary resale price, or the retail price in effect at any dealer.

Paragraph 1. Respondent totes incorporated is a corporation organized, existing and doing business under and by virtue of the laws of the State of Ohio, with its office and principal place of business located at 10078 East Kemper Road, Loveland, Ohio.

PAR. 2. Respondent is now, and for some time last past, has been engaged in the manufacture, advertising, offering for sale, sale and distribution of rubber footwear, umbrellas, hats, scarfs and other wearing apparel.

PAR. 3. Respondent maintains, and has maintained, a substantial course of business, including the acts and practices as hereinafter set forth, which are in or affect commerce, as "commerce" is defined in the Federal Trade Commission Act.

PAR. 4. Respondent sells and distributes its products directly to more than 3,000 retail dealers located throughout the United States who in turn resell respondent's products to the general public.

PAR. 5. In the course and conduct of its business, and at all times mentioned herein, respondent has been, and now is, in substantial competition in or affecting commerce with corporations, firms and individuals engaged in the manufacture, advertising, offering for sale, sale and distribution of merchandise of the same general kind and nature as merchandise manufactured, advertised, offered for sale, sold and distributed by respondent.

PAR. 6. In the course and conduct of its business as above described, respondent has for some time last past administered and conducted cooperative advertising programs which contain a limitation or restriction denying cooperative advertising credits or allowances to dealers for advertisements which do not feature respondent's suggested retail prices.

PAR. 7. The administering or conducting by respondent of cooperative advertising programs with the limitation or restriction described in Paragraph Six hereinabove has the capacity, tendency and effect of establishing, maintaining, stabilizing or otherwise illegally influencing the resale prices of dealers in respondent's products, and has had and still has the capacity, tendency and effect of hindering, suppressing or eliminating competition between or among those dealers selling respondent's products.

PAR. 8. The aforesaid acts and practices of respondent have been and are now having the effect of hampering and restraining competition in the resale and distribution of respondent's products, and, thus, are to the prejudice and injury of the public, and constitute unfair methods of competition in or affecting commerce or unfair acts and practices in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act. The acts and practices of respondent as herein alleged, are continuing and will continue in the absence of the relief herein requested.

Decision and Order

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the San Francisco Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act; and

The respondent, its attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent totes incorporated is a corporation organized, existing and doing business under and by virtue of the laws of the State of Ohio, with its office and principal place of business located at 10078 East Kemper Road, in the City of Loveland, State of Ohio.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

Order

For the purposes of this Order, the following definitions shall apply:

"Product" is defined as any item which is manufactured, offered for sale or sold by respondent.

"Dealer" is defined as any person, partnership, corporation or firm which is authorized by respondent to purchase any product.

"Resale Price" is defined as any price, price floor, price ceiling, price range, or any mark-up, formula or margin of profit used by any

dealer for pricing any product. Such term includes, but is not limited to, any retail price suggested or established by respondent, any customary resale price, or the retail price in effect at any dealer.

It is ordered, That respondent totes incorporated, a corporation, its successors and assigns; and respondent's officers, agents, representatives and employees, directly or indirectly, or through any corporation, subsidiary, division or other device, in connection with the designing, implementing, conducting, administering or auditing of any cooperative advertising program, or portion thereof, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, shall cease and desist from:

I

1. Threatening to withhold or withholding cooperative advertising credits or allowances from any dealer, or limiting or restricting the right of any dealer to participate in any cooperative advertising program for which it would otherwise qualify, because of the resale price at which said dealer advertises or sells any product, or proposes to advertise or sell any product.

2. Threatening to withhold or withholding cooperative advertising credits or allowances from any dealer, or limiting or restricting the right of any dealer to participate in any cooperative advertising program for which it would otherwise qualify, because said dealer has advertised or sold, or proposes to advertise or sell, any product using or featuring any resale price comparison.

II

It is further ordered, That respondent shall within thirty (30) days after service of this Order, mail under separate cover a copy of the enclosure set forth in the attached Exhibit A to each of its present accounts. Respondent, however, need not send said enclosure to any account of its "XIIX Karat," A,J, Bergren, Eastman Products, or L. P. Henryson divisions. An affidavit shall be sworn to by an official of respondent verifying that the attached Exhibit A was so mailed.

III

It is further ordered, That respondent shall forthwith distribute a copy of this Order to each of its operating divisions; and, for a period of three (3) years from the date of service of this Order, to each of its personnel, agents or representatives having sales, advertising or

policy responsibilities with respect to the subject matter of this Order.

IV

It is further ordered, That respondent notify the Commission at least thirty (30) days prior to any proposed change in the respondent, such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporation which may affect compliance obligations arising out of the Order.

V

It is further ordered, That respondent shall within sixty (60) days after service upon it of this Order, file with the Commission a report, in writing, setting forth in detail the manner and form in which it has complied with this Order.

EXHIBIT A

Dear Retailer:

totes incorporated, without admitting any violation of the law, has agreed to the entry of an Order by the Federal Trade Commission regulating its cooperative advertising programs. In connection therewith, the Company has agreed to send you this letter describing the Order.

The Order provides, among other things, as follows:

You are free to participate in, and receive reimbursement under, any totes incorporated cooperative advertising program regardless of the retail price you feature in otherwise qualifying advertisements.

If you have any questions regarding the Order or this letter, please call _____ at totes.

_____

for totes incorporated

IN THE MATTER OF

TINGLEY RUBBER CORP.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-3041. Complaint, Sept. 12, 1980—Decision, Sept. 12, 1980

This consent order requires, among other things, a South Plainfield, N.J. manufacturer of molded rubber footwear to cease withholding cooperative advertising credits or allowances, or in any way limiting or restricting dealers from participating in any cooperative advertising program because of the resale price at which the dealer has advertised or sold a product; or because the dealer has used price comparisons in the advertising and sale of a product.

Appearances

For the Commission: *Jerome S. Lamet.*

For the respondent: *Allan J. Weinschel, Weil, Gotschal & Manges,* New York City.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, as amended, 15 U.S.C. 41, *et seq.,* and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that Tingley Rubber Corp., hereinafter sometimes referred to as respondent, a corporation, has violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges as follows:

For purposes of this complaint, the following definitions shall apply:

"Product" is defined as any item which is manufactured, offered for sale or sold by respondent.

"Dealer" is defined as any person, partnership, corporation or firm which purchases any product for retail sale.

"Resale Price" is defined as any price, price floor, price ceiling, price range, or any mark-up, formula or margin of profit used by any dealer for pricing any product. Such term includes, but is not limited to, any retail price suggested or established by respondent, any customary resale price or the retail price in effect at any dealer.

"Cooperative Advertising" is defined as advertising which invites the public to purchase respondent's products at dealer's place of

business, whether the cost of the advertising is borne by respondent alone or shared by dealer and/or wholesaler and respondent.

PARAGRAPH 1. Respondent Tingley Rubber Corp. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey, with its principal office and place of business at 200 South Ave., South Plainfield, New Jersey.

PAR. 2. Respondent is now, and for some time last past, has been engaged in the manufacture, advertising, offering for sale, sale and distribution of molded rubber footwear for men, women and children. Sales by respondent for fiscal year 1978 exceeded twelve million dollars.

PAR. 3. Respondent maintains, and has maintained, a substantial course of business, including the acts and practices as hereinafter set forth, which are in or affect commerce, as "commerce" is defined in the Federal Trade Commission Act.

PAR. 4. Respondent sells and distributes its products to more than one hundred footwear wholesalers located throughout the United States who in turn resell respondent's products to dealers.

PAR. 5. Except to the extent that competition has been hindered, frustrated, lessened and eliminated, as set forth herein, in the course and conduct of its business, and at all times mentioned herein, respondent has been, and now is, in substantial competition in or affecting commerce with corporations, firms and individuals engaged in the manufacture, advertising, offering for sale, sale and distribution of merchandise of the same general kind and nature as merchandise manufactured, advertised, offered for sale, sold and distributed by respondent.

PAR. 6. In the course and conduct of its business, as above described, respondent has for some time administered cooperative advertising programs which limit or restrict the rights of dealers to obtain cooperative advertising credits or allowances for any merchandise which has been:

a. Advertised at a sale price, at a discount price, at a promotional price, at a reduced price, at an off-price, or at a mark-down.

b. Advertised at less than the suggested retail price, or at less than any minimum resale price.

c. Advertised using a price comparison.

PAR. 7. The administering by respondent of cooperative advertising programs or plans with any of the limitations or restrictions described in Paragraph Six hereinabove has the capacity, tendency and effect of establishing, maintaining, fixing, stabilizing or otherwise illegally influencing the resale prices of dealers in respondent's

products, and has had and still has the capacity, tendency and effect of hindering, suppressing or eliminating competition between or among those dealers selling respondent's products.

PAR. 8. The aforesaid acts and practices of respondent have been and are now having the effect of hampering and restraining competition in the resale and distribution of respondent's products, and, thus, are to the prejudice and injury of the public, and constitute unfair methods of competition in or affecting commerce or unfair acts and practices in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the Chicago Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act; and

The respondent, its attorneys, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent Tingley Rubber Corporation is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey, with its office and principal place of business located at 200 South Ave., in the City of South Plainfield, State of New Jersey.

2. The Federal Trade Commission has jurisdiction of the subject

matter of this proceeding and of the respondent, and the proceeding is in the public interest.

ORDER

For the purposes of this Order, the following definitions shall apply:

"Product" is defined as any item which is manufactured, offered for sale or sold by respondent.

"Dealer" is defined as any person, partnership, corporation or firm which purchases any product for retail sale.

"Resale Price" is defined as any price, price floor, price ceiling, price range, or any mark-up, formula or margin of profit used by any dealer for pricing any product. Such term includes, but is not limited to, any retail price suggested or established by respondent, any customary resale price or the retail price in effect at any dealer.

"Cooperative Advertising" is defined as advertising which invites the public to purchase respondent's products at dealer's place of business, whether the cost of the advertising is borne by respondent alone or is shared by dealer and/or wholesaler and respondent.

I

It is ordered, That respondent Tingley Rubber Corp., a corporation, its successors and assigns; and respondent's officers, agents, representatives and employees, directly or through any corporation, subsidiary, division or other device, in connection with the designing, implementing, conducting, administering or auditing of any cooperative advertising program or any other promotional assistance program, or portion thereof, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, shall cease and desist from:

1. Threatening to withhold or withholding cooperative advertising credits or allowances or any other promotional assistance payments from any dealer, or limiting or restricting the right of any dealer to participate in any cooperative advertising program or any other promotional assistance program for which it would otherwise qualify, because of the resale price at which said dealer advertises or sells any product, or proposes to advertise or sell any product.

2. Threatening to withhold or withholding cooperative advertising credits or allowances or any other promotional assistance payments from any dealer, or limiting or restricting the right of any dealer to participate in any cooperative advertising program or any other promotional assistance program for which it would otherwise

qualify, because said dealer has advertised or sold, or proposes to advertise or sell, any product using or featuring any resale price comparison.

II

It is further ordered, That respondent shall:

1. Within thirty (30) days after service of this Order, mail under separate cover a copy of the enclosure set forth in the attached Exhibit A to each of its present wholesalers and to all publications soliciting advertising for respondent's products. An affidavit shall be sworn to by an official of respondent verifying that the attached Exhibit A was so mailed.

2. Mail under separate cover a copy of the enclosure set forth in the attached Exhibit A to any person, partnership, corporation or firm that becomes a new wholesaler or solicits advertising for respondent's products within three (3) years after service of this Order.

III

It is further ordered, That respondent shall forthwith distribute a copy of this Order to all of its operating divisions, and to present or future personnel, agents or representatives having sales, advertising or policy responsibilities with respect to the subject matter of this Order, and that respondent secure from each such person a signed statement acknowledging receipt of said Order.

IV

It is further ordered, That respondent notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondent, such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporation which may affect compliance obligations arising out of the Order.

V

It is further ordered, That respondent shall within sixty (60) days after service upon it of this Order, file with the Commission a report, in writing, setting forth in detail the manner and form in which it has complied with this Order.

EXHIBIT A

Dear Wholesale Distributor/Publisher:

Tingley Rubber Corp., without admitting any violation of the law, has agreed to the entry of an Order by the Federal Trade Commission regulating its cooperative advertising programs. In connection therewith, the Company has agreed to send you this letter describing the Order.

The order provides, among other things, as follows:

1. Dealers are free to participate in any cooperative advertising program or any other promotional assistance program conducted by Tingley Rubber Corp. regardless of the retail price at which they advertise or sell any Tingley product.

2. Dealers will receive reimbursement under any Tingley cooperative advertising program or any other promotional assistance program regardless of the retail price featured in otherwise qualifying advertisements.

If you have any questions regarding the Order or this letter, please call _____ at Tingley.

_____

for Tingley Rubber Corp.

IN THE MATTER OF

TENNECO, INC.

Docket 9097. Interlocutory Order, Sept. 22, 1980

ORDER DENYING RESPONDENT'S MOTION FOR RELIEF NECESSITATED BY *EX PARTE* CONTACT WITH THE COMMISSION AND RESPONDENT'S MOTION TO DISQUALIFY COMMISSIONER PITOFSKY

On August 12, 1980, respondent, Tenneco, Inc., filed two motions alleging due process violations and procedural irregularities arising out of Commission consideration of a separate staff investigation of certain acquisitions by respondent, acquisitions that are not at issue in the present adjudicative matter. Because the issues raised by respondent in those two motions are so closely related, as are our conclusions, we find it appropriate to respond to both motions in a single order.

In one motion, respondent seeks alternative forms of relief occasioned by what it describes as improper *ex parte* contacts with the Commission by complaint counsel involving factual issues yet to be decided in the present proceeding.[1] In another, respondent moves that Commissioner Pitofsky be disqualified from participation in the decision of this appeal because, in presenting the facts of that separate merger investigation to the Commission, he allegedly prejudged certain issues in the present adjudication.[2] Complaint counsel have responded to each of these motions,[3] and Commissioner Pitofsky has submitted a response to the disqualification motion.[4]

Background

The issue central to this controversy is whether the investigation of a series of foreign acquisitions by Tenneco distinct from the acquisition in adjudication here was conducted as, and was in fact, a "separate" investigation as that term is used in Rule 4.7(f) of the Commission's Rules of Practice. Briefly, these are the relevant facts. Respondent contends that in December 1976, in response to a letter of inquiry from the Bureau of Competition, issued in order to

[1] Respondent's Motion for Relief Necessitated by Complaint Counsel's *Ex Parte* Contact with the Commission, August 12, 1980 (hereinafter "*Ex Parte* Motion").

[2] Respondent's Motion To Disqualify Commissioner Pitofsky, August 12, 1980 (hereinafter "Disqualification Motion").

[3] Opposition to Respondent's Motion for Relief Necessitated by Complaint Counsel's *Ex Parte* Contact with the Commission, September 12, 1980; Opposition To Respondent's Motion To Disqualify Commissioner Pitofsky, September 12, 1980.

[4] Decision of Commissioner Pitofsky in Response to Motion of Tenneco, Inc. To Disqualify Him from Participation in This Proceeding, September 9, 1980.

investigate whether Tenneco's acquisition of Monroe Auto Equipment Company ("Monroe") violated Section 7 of the Clayton Act and Section 5 of the FTC Act, it provided documents relating to its acquisition of five European companies involved in production and sale of exhaust system parts. In March, 1977, the Commission issued a complaint challenging Tenneco's acquisition of Monroe because of its alleged effects upon competition in replacement markets for shock absorbers and exhaust system parts. It is undisputed that that complaint did not challenge Tenneco's five foreign acquisitions. The issue is whether the five foreign acquisitions were investigated separately as a suspected violation of Section 7.

By complaint counsel's account, the file of documents regarding those foreign acquisitions was kept separate from the documents relating to the Tenneco/Monroe matter and, after separate clearance by the Department of Justice on the matter, the foreign acquisitions were investigated *separately* from the Tenneco/Monroe matter, with separate Bureau of Competition designation. Even so, certain factual information about the foreign acquisitions originally came from the Tenneco documents submitted pursuant to the letter of inquiry issued in the Tenneco/Monroe investigation. After further investigation, and during the trial of the Tenneco/Monroe acquisition, the staff recommended that the Commission issue a complaint alleging that Tenneco's acquisition of the five foreign exhaust system parts firms violated Section 7 of the Clayton Act and Section 5 of the FTC Act. It was in the normal course of presentation of that matter to the Commission for consideration that Commissioner Pitofsky made the written and oral statements about facts relating to replacement markets for shock absorbers and exhaust system parts that respondent claims prejudged similar questions of fact at issue in this adjudication. A complaint challenging the five foreign acquisitions was not issued by the Commission and the matter was closed.

The Ex Parte Communications

Respondent contends that the *ex parte* communications by staff detailed in its motions necessitate drastic forms of relief, including a) dismissal of the instant complaint *or* b) preclusion of any finding or conclusion that was the subject of improper *ex parte* communication *and* disclosure of the entire file of the now-closed investigation of the foreign acquisitions *and* c) disqualification of Commissioner Pitofsky.[5]

[5] Respondent brings this motion to the Commission, it says, in the event that the ALJ's dismissal is not affirmed. But the contentions presented raise such important and, we think, clear-cut questions going to the lawful, constitutional functioning of the Commission that we hereby dispose of them, prior to the oral argument.

We find that no relief whatsoever is necessitated, for we find in the first instance that no improper *ex parte* communications have occurred. The communications that undoubtedly occurred were quite proper and complied precisely with the Commission's procedures for treatment of such communications which themselves conform to the standards of the Administrative Procedure Act, 5 U.S.C. 552(a), 554(d), and the Due Process Clause. We also find that Commissioner Pitofsky, who has removed himself from the decision of these immediate questions, has not prejudged any issue of fact or law in this appeal and therefore should not be disqualified from participation.

Respondent argues too broadly when it says that, in the course of the Commission's consideration of the proposed complaint against Tenneco for its foreign acquisitions, "extensive" presentations were made concerning the manufacture and sale of exhaust system parts. But, in any event, it admits that presentations of this nature are not "improper" under Commission Rule 4.7(f) if they involve, *inter alia*, "the initiation, conduct or disposition of a separate investigation." Rules of Practice, Section 4.7(f). In the event of an *ex parte* communication described in Rule 4.7(b), but made in the context of a separate investigation, Rule 4.7(f) provides that the portion of the communication that relates to a fact in issue in an adjudicative proceeding is to be placed in the docket binder of the adjudicative proceeding to which it pertains. We find that the prescribed procedure was followed assiduously here.[6]

Turning to the central issue before us, we reject respondent's assertion that this adjudication and the investigation of the legality of the foreign acquisitions were the same proceeding. They were not. Respondent makes much of the similarity or even identity of some of the arguments about product and geographic markets that appear in both complaint counsel's brief in this case and the staff's memorandum to the Commission in the other investigation, but this argument is not persuasive or controlling. As we also discuss in the context of the disqualification argument, the common facts and arguments cited by respondent simply relate to fundamental and threshold determinations that arise in any antitrust matter—the relevant geographic and product markets.[7] The fact that one or more of the

[6] We note that Rule 4.7(f) does not call for the parties to the adjudicative proceeding in question to be notified that the material is in the docket binder.

[7] Respondent also cites two findings by the Administrative Law Judge (IDF 395, 465) that purportedly demonstrate that the foreign acquisitions are an issue of fact in the instant adjudication. But both of those findings relate solely to Tenneco's exploration of the possibility of acquisition of a British shock absorber manufacturer (not one of the five foreign firms) that the law judge mentions in the context of available toehold acquisition for Tenneco or Monroe. *Ex Parte* Motion, p. 20 n. 9. The five foreign acquisitions are not mentioned in those findings.

markets is involved in adjudication does not immunize the markets or the firms in them from further law enforcement scrutiny.

Respondent concedes that it does not obtain immunity from a separate Commission investigation of its conduct or its industry just because it is a party to adjudication. Its complaint is that Rule 4.7 has been violated because there has never been a "finding" that the investigation of the foreign acquisitions was "separate." But we find ample support in the record to establish that the investigation of whether Tenneco's acquisition of the five firms independently violated Section 7 and Section 5 was a separate investigation. That record evidence includes the separate staffing, separate Justice Department clearance, separate file number, separate document management, separate subject matter and the manner of compliance with Rule 4.7 itself, involving the release of factual portions of staff papers and Commission memoranda bearing on this adjudication.

The Prejudgment Argument

In addition to the foregoing, we find it unassailable that the combined functions of investigator and decisionmaker in the office of the Federal Trade Commissioner do not give rise to a denial of due process. It is the duty of the commissioners to weigh the facts of investigations of acts or practices which may violate the laws entrusted to them, in order to determine whether there is reason to believe that such a violation has occurred, in contemplation of the issuance of a complaint. Because the commissioners are purposefully appointed to terms sufficiently long to allow them to accumulate and bring to bear expertness in industries as well as in the law, *FTC v Cement Institute*, 333 U.S. 683, 701-02 (1948), it is neither unusual nor improper that they may have occasion to perform reason-to-believe analysis of a potential violation involving a company, industry or market that is the subject of on-going litigation. When this occurs, i.e., when a commissioner has ruled on a previous complaint involving certain facts or firms, he or she is not precluded from performing further statutory duties of investigation merely because a subsequent investigation involves some of those facts or firms. *Withrow v Larkin*, 421 U.S. 35 (1974); *FTC v Cement Institute*, 333 U.S. 683 (1948).

This investigative analysis of reason-to-believe is based upon *ex parte* presentation of facts, and, as noted above, Commission rules provide for disclosure of such facts where appropriate. This reason-to-believe function also necessitates tentative and preliminary conclusions, and in antitrust matters preliminary conclusions about

geographic and product markets are essential and inescapable. Prior contact with such market-related facts does not preclude the Commission from further investigations involving them. As the Supreme Court has said by way of an example more extreme than the issue before us,

> No decision of this Court would require us to hold that it would be a violation of procedural due process for a judge to sit in a case after he had expressed an opinion as to whether certain types of conduct were prohibited by law. In fact, judges frequently try the same case more than once and decide identical issues each time, although these issues involve questions both of law and fact. *Withrow v Larkin*, 421 U.S. at 48–49.

The Supreme Court has specifically upheld the constitutionality of the combination of investigative and decision-making functions in the FTC, *FTC v Cement Institute*, and has directly addressed the issue of prior Commission contact with facts that are subsequently adjudicated:

> The fact that the Commission had entertained such views as the result of its prior *ex parte* investigations did not necessarily mean that the minds of its members were irrevocably closed on the subject of the respondent's basing point practices . . . . Id. at 701.[8]

It is clear from the cautious and qualified language he used in presenting the matter of Tenneco's foreign acquisitions to the Commission that Commissioner Pitofsky was reaching only the preliminary conclusions appropriate to the reason-to-believe function. For example, he stated a) that the proposed product market "may be an appropriate one," that the foreign and domestic sales of exhaust system parts were joined "in the complaint in Tenneco I," that "it does appear that there is a strong argument in favor," and that evidence "would seem to support" the market proposal before the Commission.[9] Furthermore, the transcript of the Commission meeting on the investigation of the foreign acquisitions, which has been released and appended to Commissioner Pitofsky's response,[10] shows that he has not prejudged any issue of fact in the current adjudication.

Conclusion

For the foregoing reasons, we conclude that the discovery of

[8] Even where an agency conducted two separate, sequential investigations of an identical set of facts for two separate legal determinations, the court found no due process violation in the agency's conduct of the second hearing after reaching conclusions in the first. *Pangburn v C.A.B.*, 311 F.2d 349 (1st Cir. 1962).

[9] Respondent's Disqualification Motion, pp. 3–4.

[10] Appendix C, Decision of Commissioner Pitofsky in Response to Motion To Disqualify Him.

information about the foreign acquisition during the course of the investigation of the Tenneco/Monroe acquisition did not violate due process or any rule of the Commission, that the record establishes the separateness of the foreign-acquisitions investigation, that the presentation of the separate investigative matter to the Commission by the staff involved *ex parte* communications of the type described by subsection (f) of Rule 4.7, that such *ex parte* communications are not prohibited so long as proper procedures for their treatment are followed, that such procedures were followed, that those procedures satisfy the standards of due process and fairness under the Administrative Procedure Act, that the presentation of the subsequent matter to the Commission by Commissioner Pitofsky was proper and constitutional and that it involved no prejudgment of issues in this adjudication. Having reached these conclusions, we find that the relief requested by respondent is not warranted and is hereby denied.

Commissioner Pitofsky did not participate.

IN THE MATTER OF

THE BENDIX CORPORATION

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT AND SEC. 7 OF THE CLAYTON ACT

Docket C-3042. Complaint, Sept. 23, 1980—Decision, Sept. 23, 1980

This consent order requires, among other things, a Southfield, Mich. industrial firm engaged in four major business segments: automotive, aerospace-electronics, forestry and industrial-energy, to divest itself of the Warner & Swasey Rotating Toolholder Business and the Bendix Crush-Form Grinder Business within one year of the effective date of the order to a Commission-approved firm. Further, the order requires Bendix to maintain the businesses as viable business entities, and prohibits any diminishing of their value prior to their divestiture. The order also places a ten-year ban on the purchase of any concerns engaged in the rotating toolholder market or in the external cylindrical grinding machine market without prior Commission approval.

Appearances

For the Commission: *Robert Doyle* and *Richard Rosen.*

For the respondent: *Abe Krash, Arnold & Porter*, Washington, D.C.

COMPLAINT

The Federal Trade Commission, having reason to believe that the respondent, The Bendix Corporation ("Bendix"), a corporation subject to the jurisdiction of the Commission, has made a tender offer and has entered into a merger agreement either of which, if consummated, would violate Section 7 of the Clayton Act, as amended, 15 U.S.C. 18 and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45; that said agreement constitutes a violation of Section 5 of the Federal Trade Commission Act, as amended; and that a proceeding in respect thereof would be in the public interest, hereby issues its complaint, stating its charges as follows:

I.

DEFINITIONS

1. For purposes of this Complaint, the following definitions apply:
(a) "Machine tool" means a stationary, power-driven machine,

falling within codes 3541 and 3542 of the 1972 Standard Industrial Classification Manual, used to cut or form metal.

(b) "Rotating toolholder" means a device in which a cutting tool is secured to a machine tool for purposes of cutting excess material in the form of chips from a metal workpiece by rotation of the cutting tool against the workpiece.

(c) "External cylindrical grinding machine" means a machine tool used for shaping a cylindrical metal workpiece by bringing the exterior of the workpiece into contact with a rotating abrasive wheel, called a grinding wheel, in order to remove excess metal.

(d) "Computer numerical control unit" means an electronic unit that directs the operation of a machine tool through a series of coded instructions from a programmed computer system, and does not include programmable controllers.

(e) "Numerically controlled machine tool" means a machine tool that is operated by instruction provided by a computer numerical control unit.

II.

THE BENDIX CORPORATION

2. Bendix is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware with its principal executive offices at Bendix Center, Southfield, Michigan.

3. Bendix is a publicly traded company (NYSE) which in 1979 had sales of $3.8 billion and net assets of $2.3 billion. Bendix and its subsidiaries are engaged in four major business segments: automotive, aerospace-electronics, forest products, and industrial-energy.

4. At all times relevant herein, Bendix has been and is now engaged in commerce within the meaning of the Clayton Act, as amended, and is a corporation whose business is in or affecting commerce within the meaning of the Federal Trade Commission Act, as amended.

III.

THE WARNER & SWASEY COMPANY

5. The Warner & Swasey Company ("Warner & Swasey") is a corporation organized, existing and doing business under and by virtue of the laws of the State of Ohio with its principal executive offices at 11000 Cedar Ave., Cleveland, Ohio.

6. Warner & Swasey is a publicly traded company (NYSE) which

in 1978 had sales of $245 million and net assets of $223 million. Warner & Swasey is one of the largest producers of machine tools in the United States.

7. At all times relevant herein, Warner & Swasey has been and is now engaged in commerce within the meaning of the Clayton Act, as amended, and is a corporation whose business is in or affecting commerce within the meaning of the Federal Trade Commission Act, as amended.

IV.

ACQUISITION

8. On December 11, 1979, Bendix and Warner & Swasey entered into an agreement providing for the merger of the two companies. Pursuant to the agreement, on December 13, 1979, Bendix offered to purchase up to 45 percent of Warner & Swasey's common stock. Following the tender offer, according to the agreement, Warner & Swasey will be merged into a subsidiary of Bendix with Warner & Swasey common stock being exchanged for Bendix preferred stock. The entire transaction is valued at approximately $300 million.

V.

TRADE AND COMMERCE

9. The relevant geographic market is the United States as a whole.

10. The relevant product markets are:

(a) The manufacture and sale of computer numerical control units and submarkets thereof;

(b) The manufacture and sale of numerically controlled machine tools and submarkets thereof;

(c) The manufacture and sale of external cylindrical grinding machines and submarkets thereof;

(d) The manufacture and sale of rotating toolholders and submarkets thereof.

11. Concentration in the manufacture and sale of the relevant products is high.

12. Barriers to entry into the manufacture and sale of the relevant products are high.

13. Bendix is and for many years has been a significant supplier of computer numerical control units to actual and potential competi-

tors of Warner & Swasey and other producers of numerically controlled machine tools.

14. Warner & Swasey is a significant purchaser of computer numerical control units.

15. The market for computer numerical control units in the United States in 1978 was approximately $105 million.

16. Bendix and Warner & Swasey are and for many years have been substantial and actual competitors in the sale of external cylindrical grinding machines.

17. In 1978, the United States market for external cylindrical grinding machines was approximately $110 million.

18. Bendix and Warner & Swasey are and for many years have been substantial and actual competitors in the sale of rotating toolholders.

19. In 1979, the United States market for rotating toolholders was approximately $35 million.

VI.

EFFECTS OF THE ACQUISITION

20. The effects of the proposed acquisition may be substantially to lessen competition or tend to create a monopoly in the relevant markets enumerated in Paragraphs 9 and 10 of this complaint in the following ways, among others:

(a) actual and potential producers of computer numerical control units other than Bendix may be foreclosed from selling to a significant purchaser of computer numerical control units;

(b) actual and potential machine tool producers other than Warner & Swasey may be foreclosed from a significant source of supply of computer numerical control units;

(c) barriers to entry into each of the relevant markets will be raised;

(d) substantial actual and potential competition between Bendix and Warner & Swasey and other firms in the manufacture and sale of external cylindrical grinding machines will be eliminated;

(e) concentration in the manufacture and sale of external cylindrical grinding machines will be increased to the detriment of actual and potential competition, and the possibilities for eventual deconcentration may be diminished;

(f) substantial actual and potential competition between Bendix and Warner & Swasey and other firms in the manufacture and sale of rotating toolholders will be eliminated;

(g) concentration in the manufacture and sale of rotating toolholders will be increased to the detriment of actual and potential competition, and the possibilities for eventual deconcentration may be diminished.

VII.

VIOLATIONS CHARGED

21. The proposed acquisition set forth in Paragraph 8, if consummated, would violate Section 7 of the Clayton Act, as amended, 15 U.S.C. 18, and would violate Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45.

22. The merger agreement described in Paragraph 8 violates Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45.

Commissioners Pitofsky and Bailey did not participate.

Decision and Order

The Federal Trade Commission having initiated an investigation of the proposed acquisition of The Warner & Swasey Company (hereinafter "Warner & Swasey") by The Bendix Corporation (hereinafter "Bendix"), and Bendix having been furnished thereafter with a copy of a draft of complaint which the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge Bendix with violations of the Federal Trade Commission Act and the Clayton Act; and

Bendix, its attorneys, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by Bendix of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by Bendix that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that Bendix has violated the said Acts, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission

hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Bendix is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware with its principal executive offices at Bendix Center, in the City of Southfield, State of Michigan.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of Bendix, and the proceeding is in the public interest.

ORDER

I

It is ordered, That the following definitions shall apply herein:

(1) "Machine Tool" means a stationary, power-driven machine, falling within codes 3541 and 3542 of the 1972 Standard Industrial Classification Manual, used to cut or form metal.

(2) "Rotating Toolholder" means a device in which a cutting tool is secured to a machine tool for purposes of cutting excess material in the form of chips from a metal workpiece by rotation of the cutting tool against the workpiece.

(3) "Warner & Swasey Rotating Toolholder Business" means that part of the Balas Division of Warner & Swasey presently owned or operated by Warner & Swasey for the manufacture of rotating toolholders and includes all assets, properties, titles to property, interests, rights, and privileges of whatever nature, tangible and intangible, including, but not limited to, all real property, buildings, machinery, equipment, tools, raw materials, inventory, customer lists, trade names, patents, patent applications, trademarks and all other property of whatever description that are unique to, or necessary for, the manufacture of rotating toolholders and which are currently in existence, together with all additions, replacements, and improvements hereafter made by Warner & Swasey or Bendix prior to divestiture.

(4) "External Cylindrical Grinding Machine" means a machine tool used for shaping a cylindrical metal workpiece by bringing the exterior of the workpiece into contact with a rotating abrasive wheel, called a grinding wheel, in order to remove excess metal.

(5) "Bendix Crush Form Grinder Business" means that part of the Automation and Measurement Division of Bendix presently owned or operated by Bendix for the manufacture of crush form grinding machines and includes all assets, properties, titles to property, interests, rights, and privileges of whatever nature, tangible and

intangible, including, but not limited to, all real property, buildings, machinery, equipment, tools, raw materials, inventory, customer lists, trade names, patents, patent applications, trademarks (excluding the trade name and trademark "Bendix"), and all other property of whatever description that are unique to, or necessary for, the manufacture of crush form grinding machines and which are currently in existence together with all additions, replacements, and improvements hereafter made by Bendix prior to divestiture.

(6) "Computer Numerical Control Unit" means an electronic unit that directs the operation of a machine tool through a series of coded instructions from a programmed computer system, and does not include programmable controllers.

(7) "Numerically Controlled Machine Tool" means a machine tool that is operated by instruction provided by a computer numerical control unit.

(8) "Bendix" means The Bendix Corporation and any successor to the business of The Bendix Corporation.

(9) "Warner and Swasey" means The Warner & Swasey Company and any successor to the business of The Warner & Swasey Company.

II

It is further ordered, That Bendix, its officers, directors, agents, representatives and employees shall:

(1) Within twelve (12) months from the date this order becomes final, divest absolutely, or cause Warner & Swasey to divest absolutely, to an acquirer which meets with the prior approval of the Federal Trade Commission, the Warner & Swasey Rotating Toolholder Business, as a viable going business of the acquirer; and

(2) Within twelve (12) months from the date this order becomes final, divest absolutely, to an acquirer which meets with the prior approval of the Federal Trade Commission, the Bendix Crush Form Grinder Business, as a viable going business of the acquirer.

III

It is further ordered, That, pending the divestiture of the Warner & Swasey Rotating Toolholder Business and the Bendix Crush Form Grinder Business required by Paragraph II of this order, Bendix shall not take any action (other than sales of products in the ordinary course of business), without the consent of the Federal Trade Commission, to diminish the value of the Warner & Swasey

Rotating Toolholder Business or the Bendix Crush Form Grinder Business.

IV

It is further ordered, That, without the prior approval of the Federal Trade Commission:

(1) For the two (2) years following the date this order becomes final, Bendix shall not equip with its computer numerical control units more than ten (10) percent of the numerically controlled machine tools manufactured by Warner & Swasey; and

(2) In the third and fourth years following the date this order becomes final, Bendix shall not equip with its computer numerical control units more than twenty-five (25) percent of the numerically controlled machine tools manufactured by Warner & Swasey.

V

It is further ordered, That:

(1) Bendix shall treat in confidence and not transfer or reveal to Warner & Swasey information which any other customer for computer numerical control units transmits to Bendix, and designates as proprietary, for such period as the customer shall specify; *provided,* that Bendix shall not have any such obligation if the proprietary information (a) has already been transmitted to Bendix and Warner & Swasey by a party other than the customer, (b) is developed by Bendix or Warner & Swasey independently, (c) is already available to the general public, or (d) becomes available to the general public through no act or fault of Bendix;

(2) Warner & Swasey shall treat in confidence and not transfer or reveal to Bendix information which any other supplier of computer numerical control units transmits to Warner & Swasey, and designates as proprietary, for such period as the supplier shall specify; *provided,* that Warner & Swasey, shall not have any obligation if the proprietary information (a) has already been transmitted to Bendix or Warner & Swasey by a party other than the supplier, (b) is developed by Bendix or Warner & Swasey independently, (c) is already available to the general public, or (d) becomes available to the general public through no act or fault of Warner & Swasey; and

(3) Bendix shall enter into an agreement in writing with each of its customers for computer numerical control units, and Warner & Swasey shall enter into an agreement in writing with each of its suppliers of computer numerical control units, embodying the

undertakings of confidentiality set forth in subparagraphs (1) and (2) of this Paragraph.

VI

It is further ordered, That, for a period of ten (10) years following the date this order becomes final:

(1) Bendix shall maintain its business in computer numerical control units as an organization and profit center separate from the machine tool business of Warner & Swasey; and

(2) In order to assure the availability of Bendix as a significant supplier of computer numerical control units to actual and potential competitors of Warner & Swasey and other manufacturers of numerically controlled machine tools, Bendix shall not offer or sell computer numerical control units to Warner & Swasey on preferential terms regarding price, delivery, service, or any other terms or conditions of sale; nor shall Bendix offer or sell new computer numerical control units to Warner & Swasey, nor offer to develop new computer numerical control units for Warner & Swasey, on a basis inconsistent with Bendix' business practices with respect to other customers for computer numerical control units.

VII

It is further ordered, That Bendix shall announce generally to the trade the provisions of Paragraphs V and VI, and shall deliver a copy of this order to each of its customers for computer numerical control units and to each of Warner & Swasey's suppliers of computer numerical control units.

VIII

It is further ordered, That Bendix shall cease and desist, for a period of ten (10) years from the date this Order becomes final, from acquiring, directly or indirectly, through subsidiaries or otherwise, without the prior approval of the Federal Trade Commission, the whole or any part of the stock, share capital, or assets (other than products acquired for use or resale in the ordinary course of Bendix' business) of any corporate or noncorporate concern organized in the United States and engaged in, or the assets of which are utilized in, the manufacture or sale in the United States of

(a) rotating toolholders;

(b) external cylindrical grinding machines; or

(c) numerically controlled machine tools;

provided, that nothing in this Paragraph shall prohibit Bendix from acquiring the stock, share capital, or assets of any corporate or noncorporate concern engaged in the manufacture of numerically controlled machine tools, whose assets devoted to the manufacture of numerically controlled machine tools at the end of the year preceding such acquisition, or whose sales thereof during the year preceding such acquisition, were not in excess of ten million dollars ($10,000,000).

IX

It is further ordered, That Bendix shall, within ninety (90) days from the date this order becomes final, and every ninety (90) days thereafter until Bendix has accomplished the divestitures required by Paragraph II of this order, submit in writing to the Federal Trade Commission a report setting forth in detail the manner and form in which Bendix intends to comply or has complied with Paragraphs II and III of this order. All such reports shall include a summary of contacts or negotiations with respect to the sale of the Warner & Swasey Rotating Toolholder Business or the Bendix Crush Form Grinder Business, the identities of all parties to such contacts or negotiations, and copies of all written communications to and from such parties.

X

It is further ordered, That annually on the anniversary of the date this order becomes final, for a period of ten (10) years, Bendix shall submit in writing to the Federal Trade Commission a verified report setting forth in detail the manner and form in which Bendix intends to comply or has complied with Paragraphs IV, V, VI, VII, and VIII of this order.

XI

It is further ordered, That Bendix notify the Federal Trade Commission at least thirty (30) days prior to any proposed change in Bendix which may affect compliance obligations arising out of the order, such as dissolution, assignment or sale resulting in the emergence of a successor corporation or the creation or dissolution of subsidiaries.

Commissioners Pitofsky and Bailey did not participate.

336-345 O - 81 - 24

IN THE MATTER OF

FORD MOTOR COMPANY

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket 9105. Complaint, Jan. 10, 1978—Decision, Oct. 2, 1980

This consent order requires, among other things, a Dearborn, Mich. motor vehicle manufacturer to cease failing to supply consumers, on request, with "Technical Service Bulletins" which clearly describe engine or transmission problems that could cost over $125; preventative maintenance steps to take; and the extent of any reimbursements or free repairs. The company is required to establish a toll-free number and mail to all requesting consumers bulletins that affect their cars. Each car owner must be notified by mail whenever warranty protection covering engine, transmission or other significant problems is extended. Respondent is further required to announce the existence of its automobile information program in various national publications, and copy test all ads before publication to ensure that the required information is communicated as effectively as their regular product advertising. Additionally, the order requires that consumers be advised of the availability of the repair information and possible post-warranty reimbursement for repairs through warranty and owner manuals, dealer showroom posters, and individual mailings to all 1979 and 1980 Ford car owners. Under the terms of the order, the company is required to follow procedures to ensure reimbursement of each owner who incurred expenses for repairs prior to notification of adjustment programs; make replacement parts available to dealers; and pay all costs for parts and labor incurred by dealers in repairing specified conditions.

Appearances

For the Commission: *Richard H. Gateley, Barbara Arnold Maier, Paul D. Gandola, Robert P. Weaver, Noble F. Jones* and *David V. Plottner.*

For the respondent: *Lloyd T. Williams, Jr.* and *David R. Larrouy,* Dearborn, Mich.; *Robert L. Wald, Wald, Harkrader & Ross,* Washington, D.C.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that Ford Motor Company, a corporation, hereinafter sometimes referred to as respondent, has violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be

in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. For the purpose of this complaint, the following definitions shall apply:

"Piston scuffing" is metal to metal contact between the pistons and the cylinder walls.

A "defect" in a motor vehicle or component thereof occurs if the motor vehicle or component thereof is subject to or potentially subject to a significant number of failures in normal operation, including failures occurring under operating conditions that either are within the parameters specified by the manufacturer or reflect reasonably expected ordinary vehicle abuse or failures to maintain. For purposes of this definition, failures attributable to normal deterioration of a component as a result of age and wear are excluded.

PAR. 2. Respondent Ford Motor Company is a corporation organized, existing, and doing business under and by virtue of the laws of the State of Delaware, with its principal office and place of business located at The American Road, Dearborn, Michigan.

PAR. 3. Respondent is now, and has been, engaged in the manufacture, advertising, offering for sale, sale, and distribution of various motor vehicles.

PAR. 4. In the course and conduct of its aforesaid business, respondent causes the said motor vehicles, when sold, to be transported from its places of business located in various States of the United States to purchasers thereof located in various other States of the United States and in the District of Columbia. Respondent maintains, and at all times mentioned herein has maintained, a substantial course of trade in said products in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended.

PAR. 5. On or about February 3, 1976, if not before, respondent received information by which it knew, or had reason to believe that there was a defect, later identified as piston scuffing, in several engines manufactured by respondent, including the engine described as the 4-cylinder, 2.3-liter engine, and the engine described as the 6-cylinder, 250 c.i.d. engine.

PAR. 6. Respondent verified in or about August, 1976, if not sooner, that piston scuffing was due to inadequate lubrication of internal parts of such engines. Respondent subsequently modified said

engines, by drilling oil squirtholes to help ensure adequate lubrication.

PAR. 7. Between May 9, and July 20, 1977, respondent initiated programs to compensate purchasers whose engines developed piston scuffing. However, in many instances purchasers are not compensated. In most, if not all, instances such purchasers are not compensated because they are not aware of respondent's programs, or because of limitations upon the programs such as model year or mileage of the motor vehicle, or because dealers do not abide by the program.

PAR. 8. In the course and conduct of its business, respondent has disseminated and caused the dissemination of advertisements and other promotional materials concerning its motor vehicles in or affecting commerce by means of advertisements printed in magazines and newspapers and advertisements transmitted by television and radio stations located in various States of the United States and in the District of Columbia, having sufficient power to carry such broadcasts across state lines, and through various other outlets, including point of sale displays and materials for the purpose of inducing and which were likely to induce, directly or indirectly, the purchase of said motor vehicles.

PAR. 9. Respondent has represented, directly or by implication, through representations contained in said advertisements and other promotional materials, that its motor vehicles are durable and reliable and are built to perform well under tough operating conditions.

PAR. 10. In truth and in fact, certain models of respondent's motor vehicles or the component parts thereof are not durable and reliable and suffer or may suffer from piston scuffing, which substantially affects or may substantially affect the reliability, durability, or performance of such motor vehicles. Therefore, said representations were and are false, misleading, or deceptive.

PAR. 11. Respondent has represented, directly or by implication, by and through the offering for sale of its motor vehicles, that its motor vehicles do not have any latent defect which substantially affects the reliability, durability, or performance of such motor vehicles.

PAR. 12. In truth and in fact, in a significant number of instances, respondent's motor vehicles suffer or may suffer from piston scuffing and other latent defects which substantially affect or may substantially affect the reliability, durability, or performance of such motor vehicles. Therefore, said representations were and are unfair or deceptive.

PAR. 13. Notwithstanding its knowledge of piston scuffing, respondent is failing and has failed to disclose to prospective purchasers

and purchasers of motor vehicles with said engines information concerning the possibility of substantial damage to the engines through piston scuffing in said engines, and the nature and extent of repairs which may be necessary to correct piston scuffing. Respondent therefore is failing and has failed to disclose material facts which, if known to prospective consumers, would be likely to affect their consideration of whether to purchase a motor vehicle from respondent. Failure to disclose the aforesaid facts to present owners of affected vehicles may cause them substantial economic harm due to inability on their part to avoid or prevent substantial damage to the engines of their vehicles. Such failures to disclose are deceptive or unfair acts or practices.

PAR. 14. Respondent is failing and has failed to disclose to prospective purchasers and purchasers of motor vehicles with said engines the existence of its adjustment program and limitations thereto described in Paragraph Seven, above. Respondent therefore is failing and has failed to disclose material facts which, if known to prospective consumers, would be likely to affect their consideration of whether to purchase a motor vehicle from respondent. Failure to disclose the aforesaid facts to present owners of affected vehicles may cause them substantial economic harm. Such failures to disclose are deceptive or unfair acts or practices.

PAR. 15. The use by respondent of the aforesaid acts and practices has had, and now has, the capacity and tendency to mislead members of the consuming public who are purchasing or who have purchased substantial quantities of motor vehicles equipped with the engines described in Paragraph Five.

Therefore, the aforesaid acts and practices of respondent, as herein alleged, were and are all to the prejudice and injury of the public and constitute unfair or deceptive acts or practices in or affecting commerce, in violation of Section 5 of the Federal Trade Commission Act, as amended.

DECISION AND ORDER

The Commission having heretofore issued its complaint charging the respondent named in the caption hereof with violation of Section 5 of the Federal Trade Commission Act, as amended, and the respondent having been served with a copy of the complaint, amended thereafter by the administrative law judge, together with a notice of contemplated relief; and

The respondent, its counsel, and counsel for the Commission having thereafter executed an agreement containing a consent

order, an admission by the respondent of all the jurisdictional facts set forth in the complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Secretary of the Commission having thereafter withdrawn this matter from adjudication in accordance with Section 3.25(c) of its Rules; and

The Commission having considered the matter, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, and having duly considered the comments filed thereafter by interested persons pursuant to Section 3.25 of its Rules; and respondent having submitted a proposed modification of the definition appearing at paragraph I.10 of said consent agreement, which proposed modification was duly placed on the public record as a comment pursuant to Section 3.25(f) of the Rules and duly considered as such comment by the Commission; and respondent and Commission counsel having agreed to said proposed modification, which has been duly incorporated into the Order appearing below; now in further conformity with the procedure prescribed in Section 3.25(f) of its Rules, the Commission hereby makes the following jurisdictional findings, and enters the following order:

1. Respondent Ford Motor Company is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its executive offices and principal place of business located at The American Road, Dearborn, Michigan.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

ORDER

I

For the purposes of this order, the following definitions shall apply:

1. "Piston scuffing" is metal-to-metal contact between the pistons and cylinder walls of the engine block in: (a) 2.3 liter engines used in 1974 through 1977 model year vehicles and built by respondent prior to March 1, 1977, and (b) 200/250 CID engines used in 1975 through 1977 model year vehicles and built by respondent between September 9, 1974 and July 2, 1977.

2. "Camshaft/rocker arm wear" is surface scratching or scoring which results from metal-to-metal contact between the camshaft and rocker arms in 2.3 liter engines used in 1974 through 1978 model year vehicles and built by respondent prior to March 1, 1978.

3. "Cracked engine block" is an engine block cracking condition which results in a hairline crack in the tappet valley wall in: (a) 400-W CID engines used in respondent's 1974 through 1977 model year vehicles and containing blocks made prior to March 1, 1977, and (b) 351-M/400-C CID engines used in respondent's 1976 and 1977 model year vehicles containing blocks made prior to March 1, 1977, cast at the Michigan Casting Center.

4. "Vehicle" is a passenger car or a truck with a gross vehicle weight rating no greater than 8,500 pounds.

5. "Affected vehicles" are those which are subject to piston scuffing, camshaft/rocker arm wear, or cracked engine block, as these terms are defined in paragraphs 1, 2 and 3.

6. "Extended policy programs" are, for piston scuffing, the Ford program codes A52, A53, A56 and A57; for camshaft/rocker arm wear, Ford program codes A54 and A55; and for cracked engine block, Ford program codes A60, A61 and A62.

7. "Adjustment program" refers to extended policy programs such as those referenced in paragraph 6 or any other program under which respondent undertakes, on a uniform basis and with eligibility defined in terms of specified time-in-service and/or specified mileage limits and/or specified other terms beyond those stated in respondent's applicable warranty or warranties, to pay for all or any part of the cost of repairing, or to reimburse owners for all or any part of the cost of repairing, any engine or transmission condition, or any condition other than an engine or transmission condition that may substantially affect vehicle durability, reliability or performance, other than service provided under a safety or emission-related recall campaign. This term does not include *ad hoc* adjustments made by respondent on a case-by-case basis and not pursuant to a general commitment to pay for specified services.

8. "Engine" refers to the engine block, cylinder head, all internal engine parts, intake and exhaust manifolds.

9. "Transmission" refers to the transmission case and all internal transmission parts other than the clutch and related parts.

10. "Technical Service Bulletin(s)" is (are) the document(s) or excerpt(s) therefrom issued by the Ford Parts and Service Division pertaining to (a) repair procedures for engine or transmission conditions as to which the cost of repair exceeds the reference cost, or (b) maintenance procedures designed to avoid engine or transmis-

sion conditions as to which the cost of repair would exceed the reference cost; or, should the designation "Technical Service Bulletin(s)" to identify such document(s) or excerpt(s) be discontinued or changed, any such document(s) or excerpt(s) issued thereafter which is (are) substantially the same in content and purpose.

11. "Explanatory material" refers to a document written in a manner reasonably designed to be clear and comprehensible to prospective purchasers and owners generally, containing the following information regarding the repair or maintenance procedures described in the related Technical Service Bulletin, to the extent such information is known to respondent:

(a) a description of the condition;

(b) a description of the symptoms indicating the condition;

(c) the possible consequences of not effecting the indicated procedures for the condition, including the possible consequences of not effecting such procedures in a timely manner;

(d) the estimated cost to the consumer of any such procedures (per respondent's applicable National Average Warranty Labor Rate, respondent's Labor Time Standards Manual and respondent's suggested retail prices for parts or a national mean price for parts);

(e) the steps or possible steps that can be taken to minimize or avoid the condition, including but not limited to maintenance procedures which are specified in the owner's manual but which might otherwise be omitted by the owner;

(f) the proper repair procedure, including the use of upgraded parts, if any; if no upgraded parts exist, a statement that the procedure may have to be repeated if such is the case; and

(g) the terms of any applicable adjustment program.

12. "Dealer" or "dealers" refers to any person, partnership or corporation which, pursuant to a sales and service agreement with respondent, purchases, or receives on consignment, vehicles from respondent for resale or lease to the public, including persons, partnerships, firms or corporations owned or operated by respondent.

13. "Reference cost" means (a) for the first year after service of this order, $125.00; (b) for each succeeding year during which this order or any part thereof remains in effect, $125.00 adjusted by a ratio, the numerator of which is the most recently published monthly Consumer Price Index, and the denominator of which is the Consumer Price Index for the month in 1980 corresponding to the month of service of this order, such adjustment to be rounded to the

nearest dollar. For purposes of paragraph B(1) of section IX, the reference cost is zero.

14. "Cost of repair" refers to a calculation of expected cost to the consumer derived by adding respondent's suggested retail prices for parts or a national mean retail price for parts which are or may be required to accomplish a specified repair and respondent's applicable National Average Warranty Labor rate charges for accomplishing that repair multiplied by the time required to effectuate the repair as determined by respondent's Labor Time Standards Manual.

15. Whenever this order requires that an action be taken within a specified period of time, the month of December shall not be included in the calculation of the specified time.

II

It is ordered, That respondent, Ford Motor Company, its successors and assigns, its officers, agents, representatives, and employees, directly or indirectly or through any corporation, subsidiary, division, or device through which respondent acts in the United States, in connection with the advertising, offering for sale, sale or distribution, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, of any vehicle, do forthwith cease and desist from:

A. Failing to disclose, in a clear and conspicuous manner, in vehicle warranty information booklets, vehicle owner guides, the full-line point-of-sale catalog published by respondent for each of its vehicle divisions, and the point-of-sale catalog published by respondent for each of its vehicle lines, the following two statements:

FORD-PAID REPAIR PROGRAMS AFTER THE WARRANTY PERIOD

Sometimes Ford offers adjustment programs to pay all or part of the cost of certain repairs. These programs are intended to assist owners and are in addition to the warranty or to required recalls. Ask Ford or your dealer about such programs relating to your Ford or Lincoln-Mercury vehicle.

To get copies of any adjustment program for your vehicle or the vehicle of interest to you:

Call Ford toll-free at 1-800-000-0000

Or write Ford at:

Ford Parts & Service Division
Post Office Box ----
Dearborn, Michigan 48121

We'll need your name and address; year, make, and model vehicle, as well as engine size; and whether you have a manual or automatic transmission.

TECHNICAL SERVICE BULLETINS

All vehicles need repairs during their lifetime. Sometimes Ford issues Technical Service Bulletins (TSBs) and easy-to-read explanations describing unusual engine or transmission conditions which may lead to costly repairs, the recommended repairs, and new repair procedures. Often a repair now can prevent a more serious repair later. Ask Ford or your dealer for any such TSBs and explanations relating to your Ford or Lincoln-Mercury vehicle.

To get copies of these Technical Service Bulletins and explanations for your vehicle or the vehicle of interest to you:

Call Ford toll-free at 1-800-000-0000

Or write Ford at:

Ford Parts & Service Division
Post Office Box ----
Dearborn, Michigan 48121

We'll need your name and address; year, make, and model vehicle, as well as engine size; and whether you have a manual or automatic transmission.

* * * * * * *

B. Failing to mail or cause to be mailed, either upon written request or upon oral request received pursuant to the toll-free telephone procedure described in paragraph B of section III, to requesters in a form which may be retained:

1. information concerning any adjustment programs applicable to the vehicle(s) identified in the request;
2. Technical Service Bulletins and related explanatory material issued during the then-current model year and the two preceding model years and applicable to the vehicle(s) identified in the request; and
3. information disclosing respondent's subscription program described in paragraph A of section III.

C. Failing to furnish dealers with the information, Technical Service Bulletins and explanatory material described in paragraph B, along with a means of indexing all such materials by vehicle make, engine size and transmission type in a manner designed to facilitate access to such materials by prospective purchasers and owners on the dealers' premises.

D. Failing to recommend and urge, in writing, that dealers:

1. place the display posters referenced in paragraph F of section IV in conspicuous and accessible locations within the dealer's showroom and service payment area;

2. upon request, provide in a form which may be retained the information, Technical Service Bulletins and material described in paragraph B to the extent applicable to the vehicle(s) of interest to the requester, subject to a reasonable charge for duplication; and

3. provide ready access to all materials described in paragraph B indexed in the manner provided by respondent pursuant to paragraph C.

E. Failing to include in one of respondent's Dealer Personnel Training Tapes each model year information regarding disclosures of adjustment programs, Technical Service Bulletins and explanatory material pursuant to paragraphs A–D, advice regarding the role of dealer personnel in making such disclosures, and the importance of following such advice.

F. Failing to include in an all-dealer letter once in each 6-month period a clear and conspicuous reminder to dealers regarding disclosures of adjustment programs, Technical Service Bulletins and explanatory material pursuant to paragraphs A–D, respondent's recommendations pursuant to paragraph D, and the importance of following such recommendations.

G. Failing to continue respondent's program of issuing Technical Service Bulletins in a manner comparable to the program as it existed in the period 1977 through 1979.

H. Failing to prepare explanatory material.

III

It is further ordered, That:

A. Respondent shall implement a program, and shall disclose such program in its vehicle owner guides, whereby persons may purchase a subscription to Technical Service Bulletins and explanatory material applicable to a specified vehicle. Such subscriptions shall be offered at a price not to exceed reasonable costs.

B. Respondent shall establish and maintain a toll-free telephone system designed to accommodate the volume of calls which result from the disclosures made pursuant to this order. The system shall provide that after obtaining a caller's name, address, vehicle year, make and model, engine size and type of transmission, the personnel receiving the call shall offer to mail (and, if requested, shall then

cause to be mailed) to the caller the information, Technical Service Bulletins and material described in paragraph B of section II.

IV

It is further ordered, That:

A. Respondent shall (a) within 30 days of the adoption of any new adjustment program, notify all dealers and (b) within 120 days of the adoption of said program, subject to priority for safety or emission-related recalls, notify by first-class mail all owners of vehicles within or potentially within said program of the condition and circumstances giving rise to, and the principal terms and conditions of, said program. The notification shall include (to the extent known to respondent) the following information:

(1) a description of the condition;
(2) a description of the symptoms indicating the condition;
(3) the possible consequences of not having the condition repaired, including the possible consequences of not having the condition repaired in a timely manner;
(4) the steps or possible steps (if any) that can be taken to minimize or avoid the condition, including but not limited to maintenance procedures which are specified in the owner's manual but which might otherwise be omitted by the owner; and
(5) the principal terms and conditions of the program.

B. Respondent shall include, in all mailings to owners pursuant to paragraph A, the disclosure statements, set forth clearly and conspicuously, required in paragraph A of section II, or the substantial equivalents thereof covering the same information.

C. Within 60 days of the date of service of this order, subject to priority for safety or emission-related recalls, respondent shall mail to all owners of 1979 and 1980 model year Ford and Lincoln-Mercury vehicles, determined from respondent's North American Vehicle Information Systems (NAVIS) records, a letter explaining and promoting the existence, availability, and benefits of respondent's adjustment program and Technical Service Bulletin information systems provided for in sections II and III. Such letter shall include the disclosure statements, set forth clearly and conspicuously, required in paragraph A of section II or the substantial equivalents thereof covering the same information. A further mailing will be made, if necessary, to cover additional owners purchasing 1980 model year Ford and Lincoln-Mercury vehicles after the date of

service of this order and reported in respondent's NAVIS records prior to November 1, 1980. This further mailing will be completed by December 31, 1980, subject to priority for safety or emission-related recalls.

D. In each issue of "Ford Times" beginning with an issue published no later than 6 months after the date of service of this order, respondent shall include a full-page advertisement containing the disclosure statements set forth in paragraph A of section II or the substantial equivalents thereof concerning the same information. In one such issue published during each 6-month period following the first issue that contains said advertisement, respondent shall include an article on service and maintenance tips that include information regarding any adjustment programs and Technical Service Bulletins adopted or published during the preceding 6-month period.

E. At least 5 times in the first year after the date of service of this order, at least 3 times in the second year and at least once in each year thereafter, respondent shall place and cause to be disseminated, in the national full-circulation editions of *Time, Newsweek, U.S. News & World Report, Sports Illustrated, People* and *Reader's Digest* magazines, full-page advertisements devoted to explaining and promoting the existence, availability and benefits of respondent's adjustment program and Technical Service Bulletin information systems provided for in sections II and III. Such advertisements shall include the toll-free telephone number required by paragraph B of section III.

Prior to placement of the first such advertisement, respondent shall conduct, or cause to be conducted, copy testing of said advertisement using a population representative of potential purchasers of Ford vehicles and employing the so-called "Group Depth Interview" or "Focus Group" method of copy testing, designed and implemented in accordance with respondent's usual procedures for such research under the direction of an outside research organization or consultant generally recognized as competent and experienced in this field and used by respondent for other advertising research. Said organization or consultant shall submit to respondent a report on the effectiveness of the tested advertisement, and said advertisement shall meet respondent's obligations under this paragraph if, on the basis of said report and applying criteria customarily applied to respondent's product advertising, the advertisement effectively communicates (a) that Ford makes information available which tells consumers about unexpected repairs or repair procedures which might save a consumer money, (b) how consumers can get information on programs and bulletins, and (c) that Ford sometimes

has programs after the warranty expires under which it pays all or part of the costs of certain repairs. In the event any subsequent advertisement prepared pursuant to this paragraph differs significantly from the first advertisement disseminated in accordance with this paragraph, respondent shall conduct or cause to be conducted copy testing of such subsequent advertisement in the same manner and for the same purpose as described above.

F. Within 120 days of the date of service of this order and each 24 months thereafter, respondent shall furnish to its dealers display posters at least 30" x 40" in size explaining and promoting the existence, availability and benefits of respondent's adjustment program and Technical Service Bulletin information systems provided for in sections II and III, and including the disclosure statements, set forth clearly and conspicuously, required in paragraph A of section II or the substantial equivalents thereof covering the same information.

V

It is further ordered, That under the terms and conditions of each adjustment program respondent shall implement and follow procedures to insure reimbursement of each owner who incurred expenses for repair of the condition subject to the program prior to notification thereof, comparable to the procedures for reimbursement included in respondent's extended policy programs for piston scuffing, camshaft/rocker arm wear, and cracked engine blocks, adjusted to fit the circumstances, terms and conditions of the particular program in question.

VI

It is further ordered, That respondent shall comply with the terms of the extended policy programs for the conditions known as piston scuffing, camshaft/rocker arm wear, and cracked engine block, as such programs were in effect on January 9, 1980, and shall pay one hundred percent of the cost of parts and labor incurred by dealers to repair those conditions in affected vehicles in accordance with the procedures and subject to the terms set forth in the applicable extended policy programs for those conditions.

VII

It is further ordered, That respondent shall make upgraded replacement parts available to all dealers in quantities adequate to

meet the reasonably anticipated need for such parts to enable dealers to perform repairs pursuant to section VI and the extended policy programs referenced therein, and also pursuant to any future adjustment programs within the terms of paragraph A of section IV, subject to *force majeure,* labor disruptions, lack of productive capacity, and other causes outside respondent's control.

VIII

It is further ordered, That sections II, III, IV, V and VII shall expire 8 years after the date of service of this order; *provided,* that if at any time during which said sections remain in effect the Commission issues a final trade regulation rule imposing obligations on the automobile industry comparable to those imposed under any such section(s), such section(s) shall terminate upon the effective date of such rule, and in such event respondent shall advise the Commission of its intention to rely on any such rule as having terminated and superceded such section(s) of this order 30 days in advance of reliance thereon; *provided further,* that if at any time during which said section(s) remain in effect the Commission issues a final guide under Sections 1.5 and 1.6 of the Commission's Rules of Practice imposing obligations on the automobile industry comparable to those imposed under any such section, then the Commission shall, upon respondent's motion or upon its own motion, reopen this proceeding within 120 days of such motion and within a reasonable time thereafter vacate any such section(s) of this order unless the Commission finds that such action is not in the public interest; and *provided further,* that nothing herein shall preclude respondent at any time from moving the Commission to alter, modify, or set aside this order under the Commission's Rules of Practice.

IX

It is further ordered, That:

A. Respondent shall, within 120 days after the date of service of this order, file with the Commission a report, in writing, setting forth in detail the manner and form in which it has complied with this order.

B. During the time that sections II, III, IV, V, and/or VII remain(s) in effect, respondent shall transmit to the Commission upon request:

(1) a copy of each Technical Service Bulletin, together with any

accompanying explanatory material required by paragraph H of section II;

(2) a copy of each communication to dealers or owners regarding an adjustment program;

(3) tearsheets, together with any copy test results, of each advertisement disseminated pursuant to paragraph E of section IV; and

(4) a copy of each poster furnished to dealers pursuant to paragraph F of section IV.

C. Respondent shall, 1 year after the date of service of this order and each year thereafter that sections II, III, IV, V, and/or VII remain(s) in effect, file with the Commission a report, in writing, setting forth the following:

(1) For each condition subject to a Technical Service Bulletin:

(a) To the extent known to respondent, a description of the nature and extent of the condition, the causes of the condition, and the parts necessary to repair the condition, identifying each part by generic name and service part number.

(b) The identification of vehicles and components thereof potentially subject to each condition:

i. vehicles shall be identified by model year, car line, the inclusive dates (month and year) of manufacture, and any other information necessary to describe the vehicles.

ii. components shall be identified by generic name (*e.g.*, cylinder block), service part number, and, if applicable, the inclusive dates (month and year) of manufacture, and any other information necessary to describe the component.

(c) The total number of vehicles stated by model year and vehicle line potentially subject to each condition.

(2) For each model year and vehicle line identified pursuant to paragraph C, disclose the total number of vehicles manufactured.

(3) Unit sales of replacement parts for each component identified pursuant to paragraph C, for the affected model year(s), and for the preceding 3 model years.

D. Once during the term of this order respondent shall file with the Commission a report setting forth in good faith its best estimates of (a) the costs and benefits, to respondent and to the public, of the obligations imposed by this order, and (b) the extent to which dealers

have displayed posters furnished to dealers pursuant to paragraph F of section IV and have provided access to Technical Service Bulletins and related explanatory material furnished by respondent as required by paragraph C of section II. Said report shall be filed within 6 months of respondent's receipt of a request therefor from the Commission or its staff and said report shall cover the period from the date of service of this order until the date of this request. Respondent shall make all underlying documents and data relating to the "cost and benefits" part of said report and used in the preparation of said report available for inspection on reasonable notice by authorized representatives of the Federal Trade Commission. If copies of any such materials are requested by such representatives, respondent may, at its option, either make such materials available to such representatives for copying purposes or provide copies at either (i) rates the Commission charges for copies of materials released pursuant to the Freedom of Information Act or (ii) respondent's costs, whichever is lower.

E. Respondent shall:

(1) for 2 years after sections II, III, IV, V and VII cease to be effective, retain records that contain the information described in paragraphs B and C; and

(2) retain records relative to the manner and form of its continuing compliance with sections II, III, IV, V, VI and VII for a period of 3 years and make said records available for inspection on reasonable notice by authorized representatives of the Federal Trade Commission.

If copies of any such records are requested by such representatives, respondent may, at its option, either make such records available to such representatives for copying purposes or provide copies at either (a) rates the Commission charges for copies of records released pursuant to the Freedom of Information Act, or (b) respondent's costs, whichever is lower.

F. During the time that sections II, III, IV, V and/or VII remain in effect, respondent shall notify the Commission prior to any change in its corporate structure, such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries, or any other change in the corporation which may affect compliance obligations arising out of this order.

G. Respondent shall forthwith distribute a copy of this order to its Ford, Lincoln-Mercury, Ford Parts and Service Divisions and dealers.

336-345 O - 81 - 25

It is further ordered, That the provisions of this order shall be limited in their application to the United States.

Concurring Statement of Commissioner Robert Pitofsky

Last February, I withheld a vote on acceptance of this proposed consent order in order to have the benefit of public comments. I noted then that the order was unusual and innovative in the way in which it dealt with Ford's future responsibility to notify purchasers of any serious defects that might arise in Ford cars.

The approach of the order requires Ford to make available in the marketplace a good deal of mechanical information which consumers can use to discover their automotive problems. Magazine ads would tell consumers that the mechanical information is available in the form of technical bulletins and the bulletins would be sent to those consumers who requested them. Consumers would then have to know enough to diagnose their own mechanical problems and complain to Ford if the problem is a design defect. The order does not require direct mail notification to owners of particular models and makes of cars that they may have certain described problems—a form of consumer alert which I said in February should be more effective in notifying consumers about defects. It was recognized, however, that direct mail notification can be expensive.

All knowledgeable parties who commented on the issue of the method of future notification of serious defects—including the Center for Auto Safety and two state Attorney General's offices—thought the notification method described in the order would not work.

I continue to be skeptical that consumers will seek out the kind of mechanical information that Ford will make available and that they would be likely to understand and use that kind of technical information. Nevertheless, Ford has agreed to make technical service bulletins available on an enhanced basis and the information system could have some significant pro-consumer effects. I am therefore voting in favor of acceptance of this order largely because I think the notification system it requires might be of some value, and because the Commission should learn something about automobile defect problems in implementing and studying this order. Finally, acceptance of the other provisions of the order allows the Commission to make available immediately some important benefits to consumers. For the future, however, I continue to believe that direct mail notification to consumers will probably be essential if automo-

bile companies are to discharge their responsibility to make known the existence of serious defects in the products they sell.

IN THE MATTER OF

STANDARD OIL COMPANY OF CALIFORNIA, ET AL.

MODIFIED ORDER IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket 8827. Decision, Nov. 26, 1974—Modified Order, Oct. 7, 1980

In compliance with the decision rendered by the Court of Appeals for the Ninth Circuit on July 3, 1978, 577 F.2d 653 (1978), this modified order amends the Commission's cease and desist orders issued against an oil company and its advertising agency on November 26, 1974, 40 FR 13488, 84 F.T.C. 1401, so that they refer only to future advertising of F-310, a gasoline additive product, rather than to "any product."

MODIFIED ORDER TO CEASE AND DESIST

Respondents having filed in the United States Court of Appeals for the Ninth Circuit petitions for review of the Commission's cease and desist order issued herein on November 26, 1974; and the Court having rendered its decision modifying the Commission's order and, as so modified, affirming and enforcing the order; and the time for filing a petition for certiorari having expired and no petition for certiorari having been filed:

Now, therefore, it is hereby ordered, That the aforesaid order to cease and desist be, and hereby is, modified in accordance with the decision and judgment of the Court of Appeals to read as follows:

I.

It is ordered, That respondent Standard Oil Company of California, a corporation, its successors and assigns, its officers, representatives, agents, employees, directly or through any corporate or other device, in connection with the advertising of the additive F-310, forthwith cease and desist from:

1. Representing directly or by implication that such product:

(a) Will produce or result in motor vehicle exhaust which is pollution free or generally pollution free; or

(b) Will eliminate or reduce air pollution caused by motor vehicles; or

(c) Will eliminate or reduce emissions from all or any number or group of motor vehicles in which it is used;

or that:

(d) Such gasoline additive product has any other quality, performance ability or other characteristic; or

(e) Tests, demonstrations, research or experiments have been conducted which prove or substantiate any of said representations;

Unless and only to the extent that each and every such representation is true and has been fully and completely substantiated by competent scientific tests. The results of said tests, the original data collected in the course thereof and a detailed description of how said tests were performed shall be kept available in written form for at least three years following the final use of the representation.

2. Representing directly or by implication that:

(a) Automotive exhaust has certain observable or measurable characteristics in all or any number or group of motor vehicles when such is not the fact; or

(b) Any machines, measuring devices or technical instruments have particular characteristics or capacities when such is not the fact; or

(c) Such product has any effectiveness in reducing air pollution or any air pollutant or air pollutants without at the same time, in the same advertisement or other form of communication, conspicuously disclosing that not all of the harmful pollutants in automotive exhaust are affected by said product; or

(d) Such product will reduce any emissions of pollutants from automobile exhaust by any percentage or numerical quantity unless in connection therewith there is a clear, accurate and conspicuous disclosure of the type of vehicle which can expect to achieve reductions of such magnitude and the approximate percentage of such vehicles in the general car population.

II.

It is ordered, That respondent Standard Oil Company of California, a corporation, its successors and assigns, its officers, representatives, agents, employees, directly or through any corporate or other device, in connection with the advertising of the additive F–310, forthwith cease and desist directly or indirectly from:

1. Advertising by or through the use of or in conjunction with any test, experiment, or demonstration, or the result thereof, or any other information or evidence that appears or purports to confirm or prove, or is offered as confirmation, evidence, or proof of any fact, product characteristic or the truth of any representation, which does

not accurately demonstrate, prove, or confirm such fact, product characteristic, or representation.

2. Using any pictorial or other visual means of communication with or without an accompanying verbal text which directly or by implication creates a misleading impression in the minds of viewers as to the true state of material facts which are the subject of said pictures or other visual means of communication.

3. Misrepresenting in any manner or by any means any characteristic, property, quality, or the result of use of such gasoline additive product.

III.

It is ordered, That respondent Batten, Barton, Durstine & Osborn, Inc., a corporation, its successors and assigns, its officers, representatives, agents, employees, directly or through any corporate or other device, in connection with the advertising of the additive F–310, forthwith cease and desist from:

1. Representing directly or by implication that such product:

(a) Will produce or result in motor vehicle exhaust which is pollution free or generally pollution free; or

(b) Will eliminate or reduce air pollution caused by motor vehicles; or

(c) Will eliminate or reduce emissions from all or any number or group of motor vehicles in which it is used;

or that:

(d) Such gasoline additive product has any other quality, performance ability or other characteristic; or

(e) Tests, demonstrations, research or experiments have been conducted which prove or substantiate any of said representations;

Unless and only to the extent that respondent has a reasonable basis for such representation based upon competent scientific tests. The results of said tests and the data collected in the course thereof relied upon by respondent shall be kept available in written form for at least three years following the final use of the representation.

2. Representing directly or by implication that:

(a) Automotive exhaust has certain observable or measurable characteristics in all or any number or group of motor vehicles when such is not the fact; or

(b) Any machines, measuring devices or technical instruments have particular characteristics or capacities when such is not the fact; or

(c) Such product has any effectiveness in reducing air pollution or any air pollutant or air pollutants without at the same time, in the same advertisement or other form of communication, conspicuously disclosing that not all of the harmful pollutants in automotive exhaust are affected by said product; or

(d) Such product will reduce any emissions of pollutants from automobile exhaust by any percentage or numerical quantity unless in connection therewith there is a clear, accurate and conspicuous disclosure of the type of vehicle which can expect to achieve reductions of such magnitude and the approximate percentage of such vehicles in the general car population.

IV.

It is ordered, That respondent Batten, Barton, Durstine & Osborn, Inc., a corporation, its successors and assigns, its officers, representatives, agents, employees, directly or through any corporate or other device, in connection with the advertising of the additive F–310, forthwith cease and desist directly or indirectly from:

1. Advertising by or through the use of or in conjunction with any test, experiment, or demonstration, or the result thereof, or any other information or evidence that appears or purports to confirm or prove or is offered as confirmation, evidence or proof of any fact, product characteristic, or of the truth of any representation which does not accurately demonstrate, prove, or confirm such fact, product characteristic, or representation unless the respondent can establish it neither knew, nor had reason to know, nor upon reasonable inquiry could have known that such was the case.

2. Using any pictorial or other visual means of communication with or without an accompanying verbal text which directly or by implication creates a misleading impression in the minds of viewers as to the true state of material facts which are the subject of said pictures or other visual means of communication unless the respondent can establish it neither knew nor had reason to know nor upon reasonable inquiry could have known the true facts.

3. Misrepresenting in any manner or by any means any characteristic, property, quality, or the result of the use of such gasoline additive product unless the respondent can establish it neither knew nor had reason to know nor upon reasonable inquiry could have known that such representations are false.

It is further ordered, That respondent corporations shall forthwith distribute a copy of this order to each of their operating divisions.

It is further ordered, That respondents herein shall notify the Commission at least thirty (30) days prior to any proposed change in any of the corporate respondents such as dissolution, assignment, or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporation which may affect compliance obligations arising out of the order.

It is further ordered, That respondents shall, within sixty (60) days after service of this order upon them, file with the Commission a written report, signed by the respondents, setting forth in detail the manner and form of their compliance with the order to cease and desist.

Commissioner Pitofsky did not participate.

IN THE MATTER OF

HEUBLEIN, INC., ET AL.

FINAL ORDER, OPINION, ETC., IN REGARD TO ALLEGED VIOLATION OF SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT AND SEC. 7 OF THE CLAYTON ACT

Docket 8904. Amended Complaint, Nov. 16, 1976—Order, Oct. 7, 1980*

This order dismisses the Commission's November 16, 1976 amended complaint which alleged that the effect of Heublein, Inc.'s acquisition of a controlling interest in United Vintners, Inc. substantially lessened competition or tended to create a monopoly in the production, distribution and/or sale of wine in the United States. The Commission, in dismissing the complaint, held that the small lessening of actual competition resulting from the merger and the evidence in the record were insufficient to establish a violation of antitrust law.

Appearances

For the Commission: *Nelson M. Ishiyama, Laurence O. Masson* and *Mary L. Azcuenaga.*

For the respondent: *George J. Caspar,* Farmington, Ct.; *Richard E. Walton,* San Francisco, Ca.; *Lloyd W. McCormick, William H. Armstrong* and *Warren E. George, McCutchen, Doyle, Brown & Enersen,* San Francisco, Ca.; *J. Wallace Adair, Ralph J. Savarese, John DeQ. Briggs, III* and *Raymond A. Jacobsen, Jr., Howrey & Simon,* Washington, D.C.

AMENDED COMPLAINT

The Federal Trade Commission, having reason to believe that Heublein, Inc. (hereinafter "Heublein"), and Heublein Allied Vintners, Inc. (hereinafter "Vintners"), respondents herein, have violated the provisions of Section 7 of the Clayton Act, as amended, (15 U.S.C. 18), and that the above-named respondents, Allied Grape Growers (hereinafter "Allied"), and United Vintners (hereinafter "United"), respondents herein, have further violated the provisions of Section 5 of the Federal Trade Commission Act (15 U.S.C. 45), through the acquisition by Heublein of a controlling interest in United, and that a proceeding in respect thereof would be in the public interest, hereby issues this amended complaint (hereinafter "complaint") pursuant to Section 11 of the amended Clayton Act and

* Original Complaint issued Nov. 27, 1972.

Section 5 of the Federal Trade Commission Act, stating its charges as follows:

I.

DEFINITIONS

1. For purposes of this complaint, the following definitions will apply:

A. *All wine.* All wine is a recognized industry term for expressing total production, distribution and/or sale statistics for table, dessert and sparkling wine. There are recognized statistical subdivisions in the wine industry, for example, imports and domestic wine or premium and standard wine. For simplification, however, the market share percentages used in this complaint are for "all wine" production, distribution or sale. [2]

B. *Table or dinner (hereinafter table) wines.* Table wines are still (non-effervescent) wine products. Their alcohol content is not over 14% by volume.

C. *Dessert or sweet (hereinafter dessert) wines.* Dessert wines are still wine products with over 14% alcohol by volume.

D. *Sparkling wines.* Sparkling wines are effervescent wine products. Their alcohol content usually ranges from 10 to 14% by volume.

II.

ACQUISITION

2. On or about September 17, 1968, as a result of negotiations commenced earlier during 1968, the Board of Directors of Allied and representatives of Heublein reached an agreement in principle whereby Heublein would acquire a controlling interest in United, a wholly-owned production and marketing subsidiary of Allied. The acquisition was approved by Allied's membership in late 1968. On or about February 21, 1969, the acquisition was completed, giving Heublein a controlling interest in United through its control of Vintners.

3. Under the terms of the acquisition agreement, Allied's members received shares of Heublein common stock valued at approximately $7,521,000, Heublein Series A preferred stock valued at approximately $20,319,000, and Heublein Series B preferred stock valued at approximately $5,000,000. Pursuant to the acquisition agreement, United was converted to a corporation with the same name and became a wholly-owned subsidiary of Vintners, a corpora-

tion organized for the purpose of this transaction. The members of Allied received all of the Class B common stock of Vintners, constituting 18% of Vintners' outstanding stock, and Heublein received all of Vintners' Class A common stock, which constituted 82% of Vintners' outstanding stock. The members of Allied formed a second non-profit cooperative association with the same name, succeeding to all assets and liabilities of its predecessor. All outstanding shares of Vintners' Class B common stock were contributed by the members to the new Allied organization.

III.

HEUBLEIN, INC.

4. Respondent Heublein is a corporation organized, existing and doing business under and by virtue of the laws of the State of Connecticut, with its principal office and place of business located at 330 New Park Ave., Hartford, Connecticut. At all times relevant herein, Heublein sold and shipped its products in interstate commerce and thus it was engaged in commerce as "commerce" is defined in the Clayton Act, and was engaged in or its business affected commerce as "commerce" is defined in the Federal Trade Commission Act. [3]

5. At the time it acquired a controlling interest in United, Heublein was a major industrial corporation, a national leader in the sale of alcoholic beverages and a seller of specialty food products. Net sales for its fiscal years ending June 30 were: $1,466,095,000 in 1975; $1,283,002,000 in 1974; $1,013,115,000 in 1973; $922,190,000 in 1972; $629,845,000 in 1971; $586,295,000 in 1970; $523,799,000 in 1969 and $487,767,000 in 1968. In 1969, Heublein was the fifth largest company in the United States selling alcoholic beverages.

6. Notable among Heublein's distilled liquor products are vodka, gin, rum, tequila, Scotch and Canadian whiskey. Its Smirnoff vodka is the largest selling brand of vodka in the country and the second largest selling brand of liquor made in the United States. Heublein originated and continues to dominate the growing domestic market in the production and sale of prepared cocktails.

7. At the time of the acquisition of a controlling interest in United, Heublein was a competitor in the wine industry. Although its sales of wine produced in the United States were small, Heublein was a major wine importer. In 1967, it imported 1,100,000 gallons. This was approximately 5% of all the wine imported into the United States. Lancer's Vin Rose', produced in Portugal, was the nation's leading imported table wine in 1968 and continues to be one of the

nation's leading imported table wines. Heublein has had world distribution rights for this product since 1965. In addition, it was and is the sole importer of Harvey's Sherries & Ports, a line of dessert wines. Harvey's Bristol Cream Sherry was and is the leading imported sherry in the United States. Heublein also imported the Bertani line of wines from Italy, the Vinya and Quinta wines from Portugal and many others.

8. Since purchasing a controlling interest in United in February 1969, Heublein has expanded the company's production facilities, number of wine products and vineyard acreage. In addition, in June 1969, Heublein acquired the Beaulieu Vineyard of Napa, California and its distributor affiliate (hereinafter Beaulieu). Although small, Beaulieu is regarded as one of the nation's best wineries. For the year prior to the acquisition, it had sales of $1,589,087. Also, in 1969, half of the members of the St. Helena Cooperative of St. Helena, California agreed to divert their grapes from the St. Helena Winery to United. Further, in 1969 Heublein began the annual Premiere National Auction of Rare Wines. In addition to selling rare wines, the auction also sells "futures" in anticipated production of Heublein's wines. Finally, Heublein purchased Regina Grape Products Co. of Etiwanda, California in January 1971. Regina is primarily a producer of wine vinegar.

9. Heublein is an aggressive merchandiser and distributor of its products. It is one of the nation's major advertisers with an expenditure of approximately $35,000,000 in 1970 and $103,700,000 in 1975. In 1970 it was the second largest advertiser among companies in the liquor business. In 1975 it was the largest such advertiser. [4] Heublein's budget for its wine advertising is both substantial and expanding. Heublein distributes its alcoholic beverage products to state liquor agencies in the 18 states that monopolize the sales of such products and to approximately 600 independent wholesale distributors in the remaining 32 states, the District of Columbia and the territories of the United States.

IV.

ALLIED GRAPE GROWERS

10. Respondent Allied is an incorporated agricultural cooperative association organized, existing, and doing business under and by virtue of the laws of the State of California, with its principal office and place of business in Fresno, California. At the time of the sale of a controlling interest in United, respondent Allied was in the business of acquiring grapes in California and other states and

producing and marketing wines made therefrom through its wholly-owned subsidiary United. Said wines were sold throughout the United States. Since the sale of a controlling interest in United, respondent Allied has been engaged in the business of acquiring grapes in California and other states for sale to United for the production of wine to be sold throughout the United States. Therefore, at all times relevant herein, Allied was engaged in or its business affected commerce as "commerce" is defined in the Federal Trade Commission Act.

11. As a result of its agreements with Heublein, Allied retains an 18% interest in United through its ownership of shares in Vintners, the sole shareholder of United.

12. Allied claims the contractual right to designate 8 members or 40% of the authorized number of directors of United, whichever is greater, for whom Vintners is obligated to vote. At the present time, eight members of the United board of directors are designees of Allied.

V.

UNITED VINTNERS, INC.

13. Prior to its acquisition by Heublein, respondent United was a wholly-owned subsidiary of Allied, an incorporated agricultural cooperative association organized, existing and doing business under and by virtue of the laws of the State of California. United is now a corporation organized, existing and doing business under and by virtue of the laws of the State of California. At all times relevant herein, United has had its principal office and place of business at 601 4th St., San Francisco, California. At the time of the acquisition, United was the sole operating entity of Allied, as all of Allied's production and marketing assets were held by United. When control of United was acquired by Heublein, United continued to hold and operate substantially all of said assets. At all times relevant herein, United sold and shipped its products in interstate commerce and thus it was engaged in commerce as "commerce" is defined in the Clayton Act and was engaged in or its business affected commerce as "commerce" is defined in the Federal Trade Commission Act. [5]

14. At the time of its acquisition, United was the nation's second largest seller of wine products. Net sales for its fiscal years ending August 31 were: $96,009,189 in 1968; $91,026,634 in 1967; and $86,231,076 in 1966.

15. Prior to its acquisition, United crushed the grapes delivered by Allied's approximately 1,600 members and processed and distrib-

uted the resulting wine. It also purchased some grapes from non-members. Approximately 30% of United's distribution was done through its own wholesale operations. The remainder of its sales were made by about 370 independent wholesale distributors. Allied retained a portion of the proceeds from the wine sales as a part of its capital fund and distributed the remainder to its members in proportion to the market value of the grapes each had delivered. Although the acquisition has caused some change in the procedure for determining grower compensation, United's function of crushing grapes, producing wine and distributing it has remained basically unchanged.

16. At its various wineries, United produces wines of all types, including table, dessert and sparkling. Most of these products are sold under brand names owned by United, for example, Italian Swiss Colony and Inglenook.

17. Subsequent to the acquisition, Heublein has expanded United's assets. A new glass plant near United's winery at Madera, California provides most of United's bottle requirements. In addition, a new plant for producing sparkling wines has been completed at Madera. The new facility doubled United's capacity for producing such wines. Finally, Heublein has delegated responsibility for the distribution of some of its imported wines to United.

VI.

HEUBLEIN ALLIED VINTNERS, INC.

18. Respondent Vintners is a corporation organized, existing and doing business under and by virtue of the laws of the State of California, with its principal office and place of business at 604 4th St., San Francisco, California. Vintners was organized for the purpose of this acquisition and all of its stock is held by Heublein and Allied. Its sole asset is 100% of the stock of United. Through United, Vintners is in the business of producing and marketing wines throughout the United States. Since its formation, Vintners has been engaged in commerce as "commerce" is defined in the Clayton Act, and has been engaged in or its business affected commerce as "commerce" is defined in the Federal Trade Commission Act.

VII.

TRADE AND COMMERCE

19. The product markets affected by Heublein's acquisition of a controlling interest in United are wine production, distribution and/or [6]sale generally, as reflected by "all wine" statistics, and wine's three product subcategories: table, dessert and sparkling; all of which are concentrated and nation-wide in geographic scope.

20. Wine sales in the United States are in the midst of a major expansion. They have increased from 145,186,000 gallons in 1955 to 267,084,000 in 1970 and to 367,574,000 gallons in 1975. Sales of table and sparkling wines by California wineries, wineries in other states and importers have all shared in the expansion. Sales of dessert wines, however, have decreased since 1955.

21. Wine sales in the United States are dominated by two wineries. In 1967–68, E. & J. Gallo Winery (hereinafter Gallo) and United made over 40% of the wine sales in the United States. Gallo's sales were slightly higher than United's. The third largest wine seller, Roma Wine Company (hereafter Roma), had less than 4% of the market.

22. An even higher concentration exists among California wineries that produce over 70% of the wine sold throughout the United States. In 1967–68, Gallo and United's production accounted for almost 60% of the wine produced in California and commercially sold throughout the United States. Roma, the third largest California producer, had less than 5% of California's national wine sales.

23. There are major barriers to entry to any firm wishing to make a significant entrance into the wine business. New winery equipment and the grapes for wine production are expensive. In addition, the return on investment is slow. The high cost of advertising presents a second barrier to any winery wishing to sell on a national or even regional basis. Consumer appeal, created by advertising, is an important element in the marketing of wine products.

24. Distribution represents another barrier to entry. Liquor distributors are selectively licensed, if not directly controlled, by state governments. Each state, the District of Columbia and the federal government have their own laws regulating liquor distribution. Thus, a winery is more limited in the distribution channels it may select than a non-liquor company. In addition, there is always the potential that a liquor company will require an independent wholesaler to carry and/or promote a full line of its liquor and wine

products. A wine company, not possessing such leverage, is at a disadvantage.

VIII.

EFFECT OF THE ACQUISITION

25. The effect of the acquisition by Heublein of a controlling interest in United may be substantially to lessen competition or to tend to create a monopoly in the production, distribution and/or sale of wine and its three product subcategories in the United States, [7] in violation of Section 7 of the Clayton Act, as amended; and the effect of the agreement by which Heublein, Allied and Vintners undertook to eliminate the actual and potential competition between Heublein and United may be to restrain trade unreasonably, and to hinder or have a dangerous tendency to hinder competition unduly, thereby constituting an unfair act and practice in commerce, in violation of Section 5 of the Federal Trade Commission Act. These effects may occur in the following ways:

A. Actual and substantial potential competition in the production, distribution and sale of wine may have been eliminated; high levels of concentration may be increased.

B. The entry and growth of new wineries and the expansion of existing wineries may have been retarded, limited, discouraged or even prevented.

C. Independent wineries may have been retarded, limited, discouraged or even prevented from purchasing better quality wine grapes as well as vineyard acreage for their production.

D. Independent wineries may have been deprived of an opportunity to compete for distribution rights and, thereby, ultimate sales to consumers to the detriment of the general purchasing public.

E. Mergers between potential entrants and viable wineries may result from the anticompetitive pressures resulting from Heublein's acquisition of a controlling interest in United.

F. Mergers between actual competitors producing and selling wine may result from the anticompetitive pressures resulting from Heublein's acquisition of a controlling interest in United.

IX.

VIOLATION

By reason of the foregoing, Heublein's acquisition through Vintners of a controlling interest in United, constitutes a violation of

Section 7 of the Clayton Act, as amended, and the agreement among Heublein, Allied and Vintners by which the acquisition was accomplished, constitutes a violation of Section 5 of the Federal Trade Commission Act.

Initial Decision by Alvin L. Berman, Administrative Law Judge

July 2, 1979

Preliminary Statement

The Commission's amended complaint, issued in November 1976, charged that Heublein, Inc. ("Heublein") and Heublein Allied Vintners, Inc. ("Vintners") violated Section 7 of the Clayton Act, as amended, (15 U.S.C. 18), and that Heublein, Vintners, Allied Grape Growers ("Allied") and United Vintners, Inc. ("United") violated the provisions of Section 5 of the Federal Trade Commission Act (15 U.S.C. 45) in connection with the acquisition by Heublein of a controlling interest in United.[1]

In its complaint, the Commission defined the relevant market as "all wine" which encompassed the total production, distribution and/or sales statistics for "table", "dessert" and "sparkling" wines which, in turn, were alleged to be recognized statistical subdivisions of the "wine industry". Table (or dinner) wines were defined as still (non-effervescent) wine products with alcohol content of not over 14 percent by volume; dessert (or sweet) wines were defined as still wine products with over 14 percent alcohol content by volume; and sparkling wines were defined as effervescent wine products with an alcohol content usually ranging from 10–14 percent by volume.

The challenged acquisition was alleged to have been consummated on or about February 21, 1969. Following is a summation of the specific allegations.

Heublein is a corporation organized, existing and doing business under and by virtue of the laws of the State of Connecticut, with its principal office and place of business located in Hartford, Connecticut. At all relevant times, it was engaged in commerce or its business affected commerce as "commerce" is defined in the Federal Trade Commission Act.

At the time of the acquisition, Heublein was a major industrial corporation, a national leader in the sale of alcoholic beverages

[1] The original complaint, issued in November 1972, had named only Heublein as a respondent and had charged it only with violation of Section 7 of the Clayton Act by reason of its acquisition of a controlling interest in United.

(being the fifth largest company in the United States so engaged) and a seller of specialty food products. Among its distilled liquor products was Smirnoff Vodka, the largest selling brand of vodka in the country and the second largest brand of liquor produced in the United States. Heublein originated and dominates the growing domestic market in the production and sale of prepared cocktails. In addition to selling a small amount of wine [3]produced in the United States, Heublein was a major wine importer. Its imports included Lancers Vin Rose which was produced in Portugal and was the nation's leading imported table wine in 1968. It continues to be one of the nation's leading imported table wines. Heublein was and is the sole importer of Harveys Sherries and Ports, a line of dessert wines which includes Harveys Bristol Cream Sherry which was and is the leading imported sherry into the United States.

Heublein is an aggressive merchandiser and distributor of its products. It is one of the nation's major advertisers. It was the second largest advertiser among companies in the liquor business in 1970 and the largest such advertiser in 1975. Heublein's budget for wine advertising is both substantial and expanding. It distributes its alcoholic beverage products to state liquor agencies in the 18 states that monopolize the sale of such products and to approximately 600 independent wholesale distributors in the remaining 32 states, in the District of Columbia, and in the territories of the United States.

Allied Grape Growers is an incorporated agricultural cooperative association organized, existing and doing business under and by virtue of the laws of California with its principal office and place of business in Fresno, California. At the time of its sale to Heublein of the controlling interest in United, Allied was in the business of acquiring grapes in California and other states and producing and marketing wines made therefrom through United, its wholly-owned subsidiary. At all times relevant herein, Allied was engaged in commerce or its business affected commerce, as "commerce" is defined in the Federal Trade Commission Act.

Prior to the acquisition of the controlling interest of United by Heublein, United was a wholly-owned subsidiary of Allied. United was the sole operating entity of Allied; all of Allied's production and marketing assets were held by United. At all times relevant herein, United had its principal office and place of business in San Francisco, California, was engaged in commerce as "commerce" is defined in the Clayton Act and was engaged in or its business affected commerce as "commerce" is defined in the Federal Trade Commission Act.

At the time of its acquisition, United was the nation's second

largest seller of wine products. United crushed the grapes delivered by Allied's approximately 1,600 members and processed and distributed the resulting wine. It also purchased some grapes from nonmembers. Approximately 30 percent of United's distribution was accomplished by its own wholesale operations with the remainder through about 370 independent wholesale distributors. Since the merger, United's function of crushing grapes, producing wine and [4] distributing wine products has remained basically unchanged. United produces wines of all types, including table, dessert and sparkling, and sells most of its products under brand names which it owns, for example, Italian Swiss Colony and Inglenook.

Heublein Allied Vintners, Inc. ("Vintners") is a corporation organized, existing and doing business under and by virtue of the laws of California with its principal office and place of business in San Francisco, California. Vintners was organized for the purpose of the acquisition and all of its stock is held by Heublein and Allied. Its sole asset is 100 percent of the stock of United. Through United, Vintners is in the business of producing and marketing wines throughout the United States and since its formation has been engaged in commerce as "commerce" is defined in the Clayton Act and has been engaged in or its business has affected commerce as "commerce" is defined in the Federal Trade Commission Act.

Under the terms of the acquisition agreement, United was converted from an agricultural cooperative association to a corporation with the same name, organized, existing and doing business under and by virtue of the laws of the State of California. It became a wholly-owned subsidiary of Vintners, the corporation organized for purpose of the transaction. Allied's members received all of the class B common stock of Vintners which amounted to 18 percent of Vintners' outstanding stock. Heublein received all of Vintners' class A common stock which constituted 82 percent of Vintners' outstanding stock. The members of Allied formed a second non-profit cooperative association with the same name which succeeded to all assets and liabilities of its predecessor. All outstanding shares of Vintners' class B common stock were contributed by the members to the new Allied organization. In summary, United, which had been a wholly-owned production and marketing subsidiary of Allied was reorganized as a for profit corporation with 100 percent of its stock owned by Vintners; and as a result of the various organizations and reorganizations recited in the complaint, Vintners was created as a corporation owning 100 percent of United with Heublein owning 82 percent of Vintners and Allied owning 18 percent.

Since the acquisition in February 1969, Heublein has expanded

United's assets and production facilities, the number of its wine products and its vineyard acreage. A new glass plant near United's winery at Madera, California, provides most of United's bottle requirements. A new plant for producing sparkling wines has been completed at Madera, doubling United's capacity for producing such wines. Heublein has delegated responsibility for the distribution of some of its imported wines to United. [5]

In June 1969, Heublein acquired the Beaulieu Vineyard of Napa, California ("Beaulieu"), and its distributor affiliate. Although small, Beaulieu is regarded as one of the nation's best wineries. Also in 1969, half of the members of the St. Helena Cooperative of St. Helena, California, agreed to divert their grapes from the St. Helena Winery to United. In 1971, Heublein purchased Regina Grapes Products Company of Etiwanda, California which is primarily a producer of wine vinegar.

The product markets alleged to have been adversely affected by Heublein's acquisition of a controlling interest in United are wine production, distribution and/or sale generally and wine's three product subcategories: table, dessert and sparkling, all of which are concentrated and nationwide in geographic scope. Wine sales are alleged to be in the midst of a major expansion with sales of table and sparkling wines by California wineries and wineries of other states and importers having shared in the expansion. Sales of dessert wines, however, have decreased since 1955.

Wine sales in the United States are alleged to be dominated by two wineries: Gallo Winery ("Gallo") and United. In 1967–68, these two companies accounted for over 40 percent of the wine sales in the United States with Gallo's sales being slightly higher than United's. The third largest wine seller, Roma Wine Company, had less than 4 percent of the market.

It is alleged that there are major barriers to entry to any firm wishing to make a significant entry into the wine business inasmuch as new winery equipment and the grapes for wine production are expensive and the return on investment is slow. A second barrier to any winery wishing to sell on a national or regional basis is the high cost of advertising. Consumer appeal, created by advertising, is an important element in the marketing of wine products. Another barrier to entry is distribution. Liquor distributors are either directly controlled or selectively licensed by state governments. Each state, the District of Columbia, and the federal government have laws regulating liquor distribution. Thus, a winery is more limited in the distribution channels it may select than a non-alcoholic beverage company. Further, there is the potential that a liquor company will

require an independent wholesaler to carry and/or promote a full line of its liquor and wine products to the detriment of competing wineries. Therefore, a wine company not possessing such leverage is at a disadvantage.

The effect of the merger was alleged as follows:

The effect of the acquisition by Heublein of a controlling interest in United may be substantially to lessen [6]competition or to tend to create a monopoly in the production, distribution and/or sale of wine and its three product subcategories in the United States, in violation of Section 7 of the Clayton Act, as amended; and the effect of the agreement by which Heublein, Allied and Vintners undertook to eliminate the actual and potential competition between Heublein and United may be to restrain trade unreasonably, and to hinder or have a dangerous tendency to hinder competition unduly, thereby constituting an unfair act and practice in commerce, in violation of Section 5 of the Federal Trade Commission Act. These effects may occur in the following ways.

A. Actual and substantial potential competition in the production, distribution and sale of wine may have been eliminated; high levels of concentration may be increased.

B. The entry and growth of new wineries and the expansion of existing wineries may have been retarded, limited, discouraged or even prevented.

C. Independent wineries may have been retarded, limited, discouraged or even prevented from purchasing better quality wine grapes as well as vineyard acreage for their production.

D. Independent wineries may have been deprived of an opportunity to compete for distribution rights and, thereby, ultimate sales to consumers to the detriment of the general purchasing public.

E. Mergers between potential entrants and viable wineries may result from the anticompetitive pressures resulting from Heublein's acquisition of a controlling interest in United.

F. Mergers between actual competitors producing and selling wine may result from the anticompetitive pressures resulting from Heublein's acquisition of a controlling interest in United. [7]

Respondents in substance denied the material allegations of the complaint. In addition, Heublein and United alleged that for a number of years competition in several segments of the wine industry has been dominated by Gallo and that prior to the challenged acquisition, United was declining competitively and, but for the acquisition, was destined to remain an ineffective competitor.

As noted above, Allied was not named as a party in the original

complaint. Allied, however, had moved for leave to intervene in order to protect its interest in United in the event divestiture were ordered, particularly in the light of a supply contract that (1) granted Allied the right to supply United's grape requirements for up to 80 years and (2) gave Allied the right of first refusal in the event Heublein were to divest itself of its interest in United. While affirming the administrative law judge's denial of Allied's application to intervene in the matter for all purposes, by order of June 26, 1973, the Commission granted Allied the right to participate in the proceeding with respect to the issue of relief. As also noted above, Allied was named as a party in the amended complaint.

Near the close of presentation of the defense by Heublein, United and Vintners (collectively referred to as "HUV"), Allied formally renounced all claims under the supply contract including the right of first refusal in the event Heublein should be required to divest itself of its interest in United. This resulted from an agreement reached among the respondents following decision in a private suit in a United States district court[2] in which Allied had sued Heublein for certain relief and Heublein had counterclaimed for, *inter alia,* relief from the supply contract. Following resolution of the private suit in favor of Heublein, Allied determined not to appeal and sold its 18 percent interest in Vintners to Heublein. Heublein then owned 100 percent of Vintners and, through Vintners, 100 percent of United. Allied abandoned all claims formerly made in this case (See RX 1248A–Z4).[3] [8]

Relying upon the foregoing, Allied, on September 13, 1978, moved that it be dismissed from the proceeding. On September 25, 1978, ruling was deferred until the initial decision. At CB 3, complaint counsel state that inasmuch as Allied no longer owns an interest in Vintners, it is no [9]longer necessary to retain Allied as a respondent

[2] *Allied Grape Growers* v. *Heublein, Inc.*, Civ. No. C-75-0456 (D. Cal., filed July 21, 1978).

[3] Among the abbreviations used herein are the following:

CB - Complaint counsel's brief (post-trial memorandum)
CP - Complaint Counsel's Proposed Findings of Fact, Conclusions of Law and Order
CPF - Complaint counsel's proposed finding in CP—followed by its number(s)
CR - Complaint Counsel's Reply to Respondents' Proposed Findings of Fact and Conclusions of Law
CRPF - Complaint counsel's proposed finding in CR—followed by its number(s)
CX - Commission exhibit, followed by its number and the referenced page(s)
HUV - Collective reference to respondents Heublein, United and Vintners
RAX - Exhibit of respondent Allied, followed by its number and the referenced page(s)
RP - HUV respondents' Proposed Findings of Fact, Conclusions of Law and Order
RPF - HUV respondents' proposed finding in RP—followed by its number(s)
RR - HUV respondents' Reply To Complaint Counsel's Proposed Findings of Fact, Conclusions of Law and Order
RRPF - HUV respondents' proposed finding in RR—followed by its number(s)
RX - Exhibit of HUV respondents followed by its number and the referenced page(s)
Tr. - Transcript of hearings, followed by the page number(s)

for the purpose of obtaining effective relief. Complaint counsel, therefore, do not oppose Allied's motion to be dismissed as a respondent.

On December 13, 1978, Vintners moved for dismissal of the complaint against it showing that, on November 9, 1978, Vintners merged into Heublein and ceased to exist. By order of January 3, 1979, ruling was deferred until the initial decision. At CB 3, complaint counsel state that, under these changed circumstances, it is no longer necessary to retain Vintners as a respondent for the purpose of obtaining effective relief and they do not oppose Vintners' motion to be dismissed as a respondent.

On December 13, 1978, United moved that it be dismissed from the proceeding showing that following, and as a consequence of, Heublein's acquisition of 100 percent of Vintners and Vintners' merger into Heublein, Heublein now owns 100 percent of United. By order of January 3, 1979, ruling was deferred until the initial decision. At CB 3, complaint counsel state that under these changed circumstances, it is not necessary to retain United as a respondent for the purpose of obtaining effective relief and they do not oppose United's motion to be dismissed as a respondent.

At RP 138–39, HUV assert that the overall all wine market was not alleged in the amended complaint as a product market but that the term was simply used for purposes of statistical reference; and that this is at odds with "complaint counsel's present theory of the case." I do not so read the complaint. An overall reading shows that it clearly treats "all wine" as a product category or market and "table", "dessert" and "sparkling" wines as submarkets or subcategories. For example, Par. 19 of the amended complaint alleges:

> 19. The product markets affected by Heublein's acquisition of a controlling interest in United are wine production, distribution and/or sale generally, as reflected by "all wine" statistics, and wine's three product subcategories: table, dessert and sparkling; all of which are concentrated and nation-wide in geographic scope.

The reference to " 'all wine' statistics" does not detract from the clear specification of product markets and submarkets. [10]

Again, Par. 25 of the complaint alleges, in part:

> The effect of the acquisition by Heublein of a controlling interest in United may be substantially to lessen competition or to tend to create a monopoly in the production, distribution and/or sale of wine and its three product subcategories in the United States, in violation of Section 7 of the Clayton Act, as amended; . . .

Further, "complaint counsel's present theory of the case" is no different from that presented by complaint counsel and contested by respondents throughout the entire trial of this matter.

Extensive hearings were held during which a large volume of testimony and documentary evidence was received. Official notice was taken of a number of matters at the request of both complaint counsel and respondents.

This initial decision is based upon the entire record including proposed findings of fact and conclusions of law and supporting memoranda filed by the parties, as well as their replies. The undersigned has also taken into account his observation of the witnesses who appeared before him and their demeanor. Proposed findings not herein adopted, either in the form submitted or in substance, are rejected either as not supported by the evidence or as involving immaterial matters. [11]

Findings of Fact[4] and Discussions

I. GROWTH IN WINE CONSUMPTION

1. In 1960 an estimated 158.1 million gallons of wine were consumed in the United States, or 1.46 gallons per adult of legal drinking age. In 1968 total United States consumption had increased to an estimated 205.1 million gallons, or 1.74 gallons per adult. 1969 adult per capita consumption of wines was 1.87 gallons for a total estimated United States consumption of 225.5 million gallons. In 1977 an estimated 390.4 million gallons of wine were consumed in the United States, representing an adult per capita consumption rate of 2.69 gallons (1978 Wine Marketing Handbook, p. 20; officially noticed per order dated September 27, 1978).

2. Consumer expenditures in 1960 for wine in the United States were estimated to be $751 million, climbing to an estimated $1,053 million in 1968 and $1,184 million in 1969. Consumer expenditures in the United States for wine in 1977 reached an estimated $3 billion dollars (1978 Wine Marketing Handbook, p. 20; officially noticed per order dated September 27, 1978).

3. Wine consumption in the United States is skewed towards individuals under 50 years of age (CX 125Z–42, Z–44). The greatest wine usage level is among households where the household head is 25 to 49 years of age (CX 231V), although there is some evidence that those 21–24 years of age consume 20–50 percent more wine per capita than do their older counterparts (CX 125Z–44).

4. A 1970 Bank of America study forecast that 40 million young

[4] Findings of fact, for the most part, are made in numbered paragraphs. Discussions and applications of findings, as well as consideration of legal and other matters, appear where deemed appropriate. Some follow particular findings which pertain thereto; others follow all of the numbered findings. Findings which appear in unnumbered paragraphs are, nevertheless, findings.

adults will have reached drinking age during the decade of the 1970's and will make up more than 27 percent of the adult United States population in 1980, and, of the adult population of 145 million in 1980, 70 million will have acquired their wine tastes during the 1960's and 1970's (CX 288B). [12]

5. The American wine drinking public has become more and more attuned to drinking table wine (CX 366J). The 1976 edition of *Impact,* a wine industry trade publication, summarized: "Table wine has come of age in the United States. Americans, particularly those in the 25–35 age group, are beginning to drink wine as an inherent part of their life style" (CX 367N).

6. The Bank of America's 1970 publication stated: "[T]he bank and the industry are in complete agreement that the popularity of wine in American cultural, culinary, and ceremonial tastes and preferences is accelerating unmistakably" (CX 288A).

II. THE PARTIES

A. Heublein

7. Heublein is a corporation organized, existing and doing business under and by virtue of the laws of the State of Connecticut, with its principal office and place of business located at Farmington, Connecticut (Amended Complaint and Heublein's Answer, ¶ 4).

8. Heublein sells its products nationwide (CX 4). At all times relevant herein, Heublein sold and shipped its products in interstate commerce and was thus engaged in commerce as "commerce" is defined in the Clayton Act, and was engaged in or its business affected commerce as "commerce" is defined in the Federal Trade Commission Act (Amended Complaint and Heublein's Answer, ¶ 4).

9. Heublein was incorporated under the laws of Connecticut in 1915. It was the successor to a family business founded in the 1860's. It became a public corporation in 1959 (CX 3A, 56Z–4; Tr. 3920, 4022–23).

10. Heublein entered the vodka business in 1939 when it purchased the American Smirnoff Company. At that time, American Smirnoff was selling 6,000 cases of vodka a year in this country (Tr. 3975).

11. In the early 1940's Heublein built a vermouth plant in Hartford, Connecticut (Tr. 3981).

12. In 1957, Heublein obtained the exclusive agency for importing the Harveys line of ports and sherries (CX 48L; Tr. 3985). [13]

1. Heublein, As of the Time of the Acquisition, Was a Major Industrial Corporation and National Leader in the Sale of Alcoholic Beverages and a Seller of Food Products

13. In 1966, Heublein entered the ranks of "Fortune's 500" largest corporations and ranked in the top 100 for its earnings growth rate. By 1967, Heublein had moved up from 371st to 346th place in terms of sales, and it ranked 76th in growth in earnings per share (CX 48E, 49G).

14. In 1968, according to Forbes Magazine's 21st annual report on American industry, Heublein led the 500 largest United States corporations in profitability, defined as a company's return on stockholders' equity. Heublein ranked fifth for its five-year average of profitability and third among the top ten companies that were "the most adroit users of capital." The magazine also noted Heublein's five-year average 21.2 percent return on total capital and 15.8 percent five-year growth in earnings per share (CX 38B).

15. In 1967, Heublein was the largest importer of wines into the United States (CX 48K). At the time of the acquisition, Heublein was the fifth largest domestic producer of alcoholic beverages (CX 55V, 327J, K).

16. In 1968, Heublein was principally engaged in the sale of spirits and beer. These products accounted for 52 percent and 39 percent, respectively, of Heublein's total sales (CX 135B, 49T). Heublein's vodka sales accounted for 2/3 of its total spirits sales. The company ranked first in the sale of vodka (CX 9T, U, V, 55T, U, V, 319J; Tr. 9289).

17. In fiscal year ending June 30, 1968, Heublein had net sales of $383,972,000, net income of $14,567,000 and earnings per share of $1.11 (CX 49T). In fiscal year 1969, the year of the acquisition, Heublein had net sales of $520,855,000, net income of $16,570,000 and earnings per share of $1.27, all adjusted to reflect the acquisition (CX 50U). Heublein's assets as of June 30, 1968, were $141,171,000 (CX 49E, U).

18. In fiscal year 1969, Heublein had record sales and earnings in the established lines of its business for the ninth consecutive year. Total sales exceeded a half billion dollars for the first time in Heublein's history, a year ahead of plan (CX 50E). [14]

19. In 1969, Heublein's stock sold at 20 times net earnings per share, which was very favorable at the time (Tr. 9166).

20. In fiscal year 1969, Heublein had a growing international business spanning more than 100 countries (CX 50E).

21. By 1967, as reported to its stockholders, Heublein had a "full

line of alcoholic beverages" including well-known whiskey imports (CX 48J).

22. In fiscal year ending June 30, 1969, Heublein spirits were distributed principally under the following brand names:

Vodka
- Smirnoff Vodka*
- Relska Vodka*
- Popov Vodka*
- Arrow Vodka*
- Koskorva Vodka*

Gin
- Milshire Charcoal Filtered Gin*

Whiskies
- Bell's Scotch Whisky
- McMaster's Scotch Whisky
- Black Velvet Canadian Whisky
- McMaster's Canadian Whisky
- Tullamor Dew Irish Whisky

Prepared Cocktails
- Heublein Cocktails*
- Heublein Banquet Cocktails*
- Club Cocktails*

Cordials, Liqueurs and Brandies
- Arrow Cordials & Flavored Brandies*
- Irish Mist Liqueur
- Bisquit Cognacs
- Felipe II Spanish Brandy

Tequila
- Jose Cuervo Tequila
- Matador Tequila

Rum
- Don Q Rum
- Eldorado Rum

Asterisks denote brands produced by Heublein (CX 55T). [15]

23. In its fiscal year ending June 30, 1969, excluding wines of United and Beaulieu, Heublein distributed wines under the following brand names:

Harveys Bristol Cream Sherry
Harveys Other Sherries and Ports
    Amontillado Cocktail Sherry
    Bristol Fino Sherry
    Bristol Milk Sherry
    The Director's Bin Port
    Gold Cap Port
    Hunting Port
    Shooting Sherry
    Tico Cocktail Sherry
Heublein Vermouth Sweet and Dry
Lancers Vin Rose
Quinta Red Table Wine
Vinya Rose Table Wine
Bertani Verona Italian Table Wines
Bouchard Pere & Fils Burgundy and Bordeaux Table Wines
Byrrh Aper
Chateau Bottled Bordeaux Table Wines
    Chateau Bouscaut (Graves)
    Chateau St. Georges (St. Emilion)
Harveys Selection Table Wines (France and Germany)
Hungarian Wines
    Tokay
    Egri Bikaver
Paul Jaboulet Aine Rhone Table Wines
Rheinhof German Table Wines
Valle Freres French Table Wines (CX 50Z-2)

24. Prior to the acquisition, Heublein was importing a number of other wines in limited quantities (Tr. 4319-23, 4339-40).

25. At the time of the acquisition, Heublein's principal beer brand was Hamm's. It also sold Waldech and Buckhorn beer and was introducing a new malt liquor under the Velvet Glove label (CX 55U).

26. At the time of the acquisition, Heublein had a line of specialty food products the principal brands of which were A.1. Sauce, Escoffier brand sauces, Snap-E-Tom tomato cocktail, Ortega sauces and chili products, and Grey Poupon mustard (CX 55V).

27. Heublein's leading alcoholic beverage was and is Smirnoff Vodka. From 6,000 cases at the time of acquisition of American Smirnoff Company in 1939 (Finding 10, *supra*), by 1968, Smirnoff sales approximated 22.4 percent of the United States vodka market.

Heublein's share of the national vodka business, including all of its vodka brands, was approximately 30.2 percent (Tr. 9291). [16]

28. Smirnoff had a record of outstanding success. Vodka consumption increased in little more than a decade from virtually nothing to 10.4 percent of total distilled spirits consumption by 1965. Smirnoff was the leader in making vodka a national favorite and contributed virtually all of the consumer promotion in the early years. By 1966, Smirnoff outsold every brand of scotch, gin and bourbon in the United States and was the fourth largest brand of any type of distilled spirits in the United States (CX 47D).

29. At the time of the acquisition, Smirnoff was the world's largest selling vodka and the second best-selling brand of liquor internationally (CX 43A, 49Q, S). In fiscal year 1968, sales of Smirnoff internationally reached four million cases (CX 49I).

30. By fiscal year 1968, Smirnoff was the third best selling distilled spirits brand in the United States and was gaining on second place (CX 49I).

31. In fiscal year 1969, Smirnoff continued to improve its position in the United States distilled spirits industry (CX 50F) and increased its overseas sales at a rate twice that in the United States (CX 50R).

32. According to the Nielsen Report, Smirnoff was the number one selling brand of all alcoholic beverages in 1977 in the three leading markets of the United States — Los Angeles, Chicago and New York (Tr. 9296–99).

33. Heublein Cocktails, reported by Heublein in 1966 to its stockholders as "undisputed leaders in the marketplace" (CX 47G), had dominated the growing prepared cocktail market since the turn of the century (CX 50I). By fiscal year 1969, they commanded more than twice the sales of the next most popular brand (CX 50J). In 1969, Heublein had approximately 50 percent of the United States market (Tr. 4995).

34. Another of Heublein's leading products was Harveys Bristol Cream Sherry (CX 46E). By fiscal year 1969, Harveys had become the leading imported sherry in the nation, accounting for one-third of all imported sherry (CX 50I). It is one of the most prestigious of all internationally known wines (CX 48K; Tr. 2893).

35. By 1966, Harveys full line of ten sherries and ports were carried in many liquor stores because the line was a "call" item (CX 48L).

36. At the time of the acquisition, Heublein's line of Arrow Cordials was the second best selling line of cordials and brandies in the country (CX 50E). [17]

37. Heublein's Lancers Vin Rose was a light, bubbly wine

packaged in a distinctive crock container, and advertised as a good choice to serve on all occasions. A Portuguese wine, Lancers Vin Rose had become a demand item in almost all restaurants and hotels. It was on more wine lists than any other imported or domestic wine (CX 48K, 49M).

38. By 1969, Lancers Vin Rose was the best selling imported wine in the United States and its sales were increasing (CX 50F).

39. In fiscal year 1969, Heublein's Jose Cuervo Tequila and Matador Tequila together accounted for more than 50 percent of the tequila market (CX 50I).

40. In fiscal year ending June 30, 1969, Heublein reported that its Consumer Products Division, formerly the Food Division (CX 49 O), had had an unusually good year with all its specialty foods (CX 50E). A.1. Sauce, for example, continued to dominate the meat sauce market (CX 50J).

2. Heublein, a Growth Company

41. Heublein at the time of the merger was described as a "growth company" by its Chief Executive Officer, Stuart Watson:

> It's been said that truly innovative growth companies are few indeed. These are the ones distinguished by a three-fold capacity. They are able to increase the growth of their existing products, and to underwrite the costs of new products and acquisitions, while increasing their over-all sales and earnings (CX 34D).

42. Heublein was able to plan what Mr. Watson termed "a major acquisition," the acquisition of United, while increasing the forward momentum of its existing business. In 1968, Heublein considered itself to be in a "unique position" to capitalize on opportunities for future growth with its line of products that included some of the fastest growing categories of foods and spirits, its expanding plants and facilities and its planning capability (CX 34G).

43. As noted in its 1968 Annual Report, "Heublein's steady growth over the years has derived from the progress of its established business and from the acquisition of others with good potential" (CX 49G). [18]

44. Heublein represented itself as a growth company. For the five-year period up to 1968, Heublein had an average annual growth rate in sales of 10 percent and an average annual growth rate in profits of 12 percent. The price per share of its common stock had risen from $8 5/8—$11 (adjusted for splits) in 1963 to $26—$40 1/4 in 1968 (CX 263; Tr. 2697).

45. Heublein's case sales of Harveys Bristol Cream Sherry had

increased 84 percent during the five-year period through 1968 and its sales of Lancers had gone up 294 percent (CX 264; Tr. 2463).

46. In the period from 1963 through 1968, Heublein had the following successes with what it termed *"new ventures":* case sales of Arrow cordials increased 62 percent; barrel sales of Hamm's Beer increased 9 percent; dollar sales of Coastal Valley Products increased 89 percent; and case sales of Lancers wine increased 294 percent (CX 265; Tr. 2476–77).

47. Heublein's case sales of Smirnoff increased 43 percent from 1963 to 1968 and the volume sales of A.1. Sauce increased 73 percent during the same period (CX 267; Tr. 2699).

48. During the same period, Heublein's dollar sales increased 52 percent, its earnings per share increased 103 percent, the market price of its stock increased 254 percent and its dividends per share increased 250 percent (CX 266; Tr. 2477, 2699, 2700).

49. As reported in Heublein's 1969 annual report, covering the fiscal year in which the acquisition took place, Heublein's Spirits and Wine Division increased "case sales and dollar volume as much as 17 percent" (CX 50F). Smirnoff Vodka set new records and continued "to exceed the growth rate of the distilled spirits industry by some 33 per cent" and to enjoy a major share of the growing United States vodka market in the face of toughening competition (CX 50F). Lancers case sales increased again and demand outstripped production (CX 50E, F). Arrow cordials and brandies "made important advances in [Heublein's] drive to overtake first place in this growing after-dinner drink category" (CX 50F). Heublein's recently introduced line of Club Cocktails, in its first full year in the national market had doubled Heublein's consumer cocktail business (CX 50E). Black Velvet, Don Q Rum and Jose Cuervo Tequila all increased in sales (CX 50E). Jose Cuervo's rate of growth tripled that of the total distilled spirits market, and Don Q sales had increased by 28 percent since that brand was acquired by Heublein (CX 50I). Harveys increased in unit sales some 22 percent (CX 50I). Heublein's sales to the transportation business grew (CX 50J), with sales of Smirnoff and Heublein Cocktails on international air carriers up 21 percent (CX 50R). Sales to the military increased 25 percent in response to an aggressive marketing effort by Heublein (CX 50J). In the Consumer Products Division, which [19]grew 20 percent in case sales (CX 50J), A.1. Sauce grew in dollar sales 20 percent over the last year, its growth over the preceding decade having been an "exceptional" 300 percent (CX 50J). Escoffier brand sauces also showed gains and Snap-E-Tom Tomato Cocktail increased 40 percent over the previous year (CX 50J, M). Grey Poupon Dijon Mustard had

increased its share of the mustard market some 33 percent in three years (CX 50M).

(a) Growth through New Products and Lines

50. Prior to the merger, Heublein had extensive research and development projects under way in food and liquor. These included the constant testing of new products of its own and of its competitors, and the development of new products (CX 46H).

51. Heublein originated the prepared cocktail at the turn of the century (CX 50I; Tr. 4994, 4995).

52. Heublein developed a new full-flavored cocktail with an alcoholic content between the Heublein full-strength cocktail and beer. It was the first pre-mixed cocktail to be packaged in a can. The product gained immediate consumer acceptance in the four states in which it was test-marketed and was introduced in the national market in fiscal year 1969. Heublein started with six flavors and introduced three more in fiscal year 1969 (CX 48I, 50I).

53. Based upon the success of Club Cocktails, Heublein introduced eight flavors of its full-strength cocktails in 8-ounce cans in fiscal year 1969 (CX 50J).

54. In fiscal year 1968, the year before the acquisition, Heublein marketed twenty new products (CX 49F).

55. Heublein introduced Smirnoff Silver to upgrade its price line and to top some of the recently imported vodkas (Tr. 4431–32).

(b) Expansions in Capacity

56. In 1969, Heublein announced that it had entered into a joint venture to build a new winery near Lisbon, Portugal (CX 50F). The agreement had been signed on October 11, 1968, when Heublein and Fonseca (Jose Maria da Fonseca Sucrs.,—Vinhos, S.A.R.L.), the supplier to Heublein of Lancers, Vinya and Quinta wines, entered into a joint venture under the name Internacional (J.S. da Fonseca Internacional—Vinhos, Limitada), to secure land and construct and operate a wine production facility capable of producing a minimum of 750,000 cases of wine per year (CX 63, [20]65E). The $1.6 million plant was capable of being expanded further as needed (CX 34G). Under a separate management agreement, Fonseca assumed the management duties of the joint venture with responsibility for production and related matters such as locating, developing and maintaining an adequate supply of grapes and wine (CX 64A–E). Heublein joined in the venture to assure an adequate supply of Lancers and to help the Fonsecas with financing (Tr. 4330). The wine

is produced by various wineries in Portugal, then finished and bottled at the Fonseca facilities (Tr. 4332). Heublein's initial investment in the facility was approximately $500,000 (Tr. 4492).

57. Heublein's ownership interest in the production facility joint venture with Fonseca is 49 percent. Its interest in the marketing joint venture with Fonseca is 51 percent (CX 56Z–10, Z–13). Heublein owns the Lancers trademark (RPF 149).

58. In fiscal year 1965, Heublein began construction of a $4,500,000 plant in Allen Park, Michigan with a 2,500,000 case per year capacity. The plant began producing Heublein spirits in 1966 and, in 1968, Heublein invested $600,000 to expand it to service growing markets (CX 38B, 46G, 47C).

59. In 1967, Heublein reported a planned multi-million dollar expansion of the Hamm's brewery in Los Angeles that would increase its capacity to 840,000 barrels per year (CX 48E). In fiscal year 1969, a 72,000 square foot loading area was added to the Hamm's St. Paul plant, and Hamm's entered into a joint venture with Continental Can to build a $1,950,000 can-producing facility (CX 50E, N, Q).

60. In fiscal year 1968, Heublein spent nearly $8 million to increase production capacity at major plants (CX 49F, G).

61. Almost immediately after acquiring United, Heublein announced plans for a new production facility for sparkling wine to be completed in 1971 (CX 50Q).

62. Heublein in 1969 engaged in an $18 million joint venture with the Indian Head Company to build a glass plant, the Madera Glass Company, to serve United. Heublein and Indian Head each contributed $2 million in equity and $1 million in operating capital. Heublein arranged for a $5 million loan from the Aetna Insurance Company and, by giving certain guarantees, was able to arrange for $6 million in additional loans from a group of banks (Tr. 9219–24, 9304). An additional $3 million was borrowed from the government (Tr. 9305). Heublein was to contribute any additional operating capital that might be needed (Tr. 9223). See Findings 217–20, *infra,* for additional details. [21]

63. The glass plant joint venture resulted in savings for United in the cost of glass (Tr. 9224). By 1972, the Madera Glass Company made a $1.8 million profit (Tr. 9226).

(c) External Growth

64. Heublein acquired a majority interest in Arrow Liqueurs Corporation in April 1964 for $6 million, and it acquired the

remaining minority interest in Arrow in June 1965. Arrow distributes Scotch and Canadian whiskeys, cordials and brandies (CX 12, 460, 47H).

65. In January 1965, Heublein, in accordance with its self-described "active acquisition program" (CX 46G), purchased Vintage Wines, Inc. for $2,125,000 (CX 61). At that time, Vintage Wines had numerous arrangements with suppliers from several foreign countries for distribution and sale in the United States of a variety of wines and certain distilled spirits (CX 62A, C, U–V), in addition to having several registered trademarks of its own (CX 62A, B, J–K). Heublein acquired the right to import these wines under a contract agreement (Tr. 4424–25). In addition, Vintage Wines had arrangements to import wines for certain retailers under the retailers' private labels (Tr. 4426–27). Lancers Vin Rose was the leading product of Vintage Wines (CX 46E, G, 351). Heublein purchased the Lancers trademark (Tr. 4289). Excluding Lancers, Vintage Wines sold about 100,000 cases of wine in 1969 (Tr. 4443). In 1968, the year prior to the acquisition of United, sales of Lancers Rose in the United States rose to approximately 360,000 cases (some 879,000 gallons) (RX 17I; Tr. 8703–04). In March of 1970, a white Lancers known as Lancers Vinho Bronco was introduced. A red Lancers, Lancers Rubio, was added in Heublein's fiscal 1974 (RPF 147).

66. In November 1965, Heublein acquired all of the common stock of the Theo. Hamm Brewing Co. (CX 47Q). Heublein's Hamm's beer operation performed well for several years (CX 47E, I, 48G, 49G, M, O). In fiscal year 1971, Hamm's was still profitable and expanding into new markets (CX 52N). Hamm's first loss was reported in fiscal year 1972 (CX 53F). Hamm's was sold in fiscal year 1974 (CX 359Y).

67. During the 1966 fiscal year, Heublein became the exclusive United States importer and distributor of Bertani Italian Wines (CX 47C).

68. During the 1966 fiscal year, Heublein secured United States rights to Grey Poupon Dijon Mustard, which it had previously manufactured and marketed under a licensing agreement (CX 48E). [22]

69. In 1966, Heublein acquired the exclusive United States rights to import and distribute Jose Cuervo, S.A., the world's largest selling brand of tequila (CX 47C, 48I).

70. In June 1967, Heublein became the sole United States distributor of Chateau St. Georges bottled Bordeaux table wines (CX 71).

71. Effective January 1, 1968, Heublein acquired, for $150,000, all of the outstanding common stock of Don Q Imports, Inc., the sole

United States distributor for the leading rum brand in Puerto Rico (CX 49K, T).

72. In October 1968, Heublein entered into a joint venture marketing company with the Fonseca family in which Heublein had a 51 percent interest (Tr. 4328). The venture was to market and sell wines worldwide (CX 67).

73. In October 1968, Heublein also entered into a formal agreement with Internacional whereunder the two companies would work together to develop and produce new Portuguese wines under trademarks originated or acquired by Heublein for sale by Heublein in the United States (CX 65H).

74. The Fonseca joint venture was very successful and the Fonseca Winery capacity has been enlarged to one or one-and-a-half million cases per year (Tr. 3957, 4333). The expansion was self-financed from the cash flow of the enterprise (Tr. 4492).

75. In fiscal year 1968, Heublein acquired exclusive long-term rights to United States sales of Black Velvet Canadian Whisky by agreement with Gilbeys (Canada) Ltd. (CX 49G, K).

76. In fiscal year 1968, Heublein acquired the United States distribution rights for Kiku-Masamune Sake, Japan's leading brand of sake (CX 49M).

77. On February 21, 1969, Heublein acquired a controlling interest in United, the acquisition challenged by the complaint in this case.

78. This was followed on June 5, 1969, by the acquisition of Beaulieu Vineyard (Tr. 331).

79. In fiscal year 1970, Heublein acquired all of the outstanding common stock of Grape Factors, Inc. (CX 52Z–3).

80. In January 1971, Heublein acquired Regina Grape Products Co., a producer of wine vinegar products (CX 52K, Z–3). [23]

81. In fiscal year 1971, Heublein merged with Kentucky Fried Chicken Corporation, whereby that company became a subsidiary of Heublein. Heublein thus obtained a strong position in the expanding fast foods market (CX 52C, Z–3).

82. In 1973, Heublein made two acquisitions in Brazil. First it acquired Drury's, an alcoholic beverage company and six months later it acquired a brandy company called Dreher (Tr. 9167).

83. In August 1973, Heublein acquired Davis Food Service, Inc. (CX 360Z–8).

84. In fiscal year 1974, Heublein Wines International was established as a unit within the Smirnoff Beverage and Import Co. In the same year, it became the exclusive United States distributor of

two lines of European wines, Cordier and Schloss Reinhartshausen (CX 359I).

(d) Growth and Diversification Policy

85. When Heublein became a public company in 1959, the underwriters thought that vodka accounted for too large a share of the company's business (Tr. 3987). Early in the 1960's, vodka accounted for approximately 75 percent of Heublein's gross sales (Tr. 3986–87).

86. Heublein was an aggressive company and it wanted to grow and diversify (Tr. 4438). At the time it acquired United, Heublein had a history of growth that it wanted to continue (Tr. 3988, 4944, 8677, 9028). Heublein proclaimed as corporate goals in fiscal year 1969 record growth in sales and earnings per share, and successful introduction of profitable new products (CX 50E).

87. By the spring of 1968, Heublein had formalized a top-level New Corporate Development group, headed by its Executive Vice President, which was responsible for growth planning through the development of new business and through acquisitions (CX 45B, 49G). Heublein's external development or acquisition program was active long before it became a formal department (Tr. 4426–31).

88. It was generally thought at Heublein that any acquisition would have to be of a company having a growth rate equal to or better than its existing business (Tr. 4392).

89. Heublein wanted to get into lines of business that it understood or could easily come to understand (Tr. 4439). [24]

90. Mr. John Martin, then Chairman of the Board and Chief Executive Officer of Heublein (Tr. 3972), testified that in the early 1960's Heublein already had an acquisition program to find new businesses and products compatible with Heublein's marketing skills, including its channels of distribution, in order to expand the kinds of businesses it was in. "We had an avaricious intention to expand our business and obviously acquisitions were part of it" (Tr. 3987–88).

91. Heublein was interested in acquiring products sold through supermarkets or the channels of distribution through which Heublein distilled spirits products were sold (Tr. 3928–29).

92. In connection with his responsibilities for external development at Heublein, Mr. Kelley, Executive Vice President, evaluated opportunities with companies in the food and beverage business. Wine was one of the areas of opportunity Heublein considered (Tr. 4945–46).

93. In 1969, Heublein generally was interested in diversifying only in the package goods or consumer goods business, but only in companies with a reasonable growth rate relative to Heublein's growth rate (Tr. 9164). Entry into the domestic wine business was the fulfillment of one of Heublein's three corporate goals. The others were record growth in sales and earnings-per-share, and the successful introduction of profitable new products (CX 50E).

94. Heublein planned to continue to grow in product categories where its marketing skills could assure success (CX 34G).

95. In about 1966, Heublein's long-range planning group decided that there were four categories they were interested in to diversify the Heublein business. One of those four categories was wine (Tr. 4461–66).

Additional findings which detail Heublein's interest in wines and in expanding in that market as well as actions taken in that regard prior to the challenged merger appear *infra* (Findings 787–94, 798, 809–28).

(e) Heublein's Expansion of Its Wine Business Subsequent to the Merger

96. On June 5, 1969, Heublein acquired Beaulieu Vineyard in California (Tr. 331).

97. Heublein also maintained its interest in developing foreign imported wines after it purchased United (Tr. 4485–86). [25]

98. In May 1969, Heublein became the sole United States distributor for the sale of the Bouchard Burgundy Wines produced by Bouchard Pere & Fils (CX 70).

99. On December 31, 1969, Heublein entered into an agreement to sell and distribute certain brands of Rhone Valley table wines produced by Jaboulet on an exclusive basis in the United States (CX 77).

100. In July 1970, United Vintners assumed the sole distribution rights in the United States for the Monimpex Hungarian wines (CX 74). In March 1973, Heublein assumed the rights for such wines (CX 75).

101. In February 1971, United Vintners became the sole distributor in the United States of German wines of Rhine origin and potentially of certain other German wines produced by Scholl and Hillebrand (CX 76).

102. In 1972, Mr. B.C. Solari, then President of United Vintners, went to several European countries to look at new wine prospects for Heublein (CX 225A–B; Tr. 4726–31). In June 1972, he reported to

Stuart Watson, Heublein's Chief Executive Officer, that he had worked out a possible arrangement for Heublein with respect to the Paterno line of wines. He also reported having spoken to the Becarro people in Italy and stated his intention to find out more about Yugoslavian products (CX 87).

103. Shortly thereafter, Heublein became the sole United States distributor of Paterno and Gancia wines under the Gancia and Mirafiore labels (CX 88–92). The wines included were Gancia and Mirafiore Asti Spumante, Vermouth, Chianti and Veronese wines and Sicilian Gold (CX 92B). Heublein also obtained a right of first refusal to 50 percent of any interest in the assets of Fabiano or any other Italian wine producer that Paterno might obtain (CX 92F, 323).

104. In January 1973, Heublein terminated Vino Chianti Ancilli, for which it had been exclusive agent, because Heublein had obtained the exclusive distribution rights in the United States for the wines noted above which were competitive to Ancilli (CX 72–73).

105. After the acquisition of United, Mr. Solari went to Brazil on Heublein's behalf to explore the possibility of raising grapes suitable for making wine (Tr. 4732–33).

106. In fiscal year 1971, Heublein introduced Vino Branco (a counterpart of Lancers Rose), Cold Duck and a cinnamon-flavored apple wine called Zapple (CX 52D). [26]

107. In fiscal year 1974, Heublein introduced Lancers Rubeo and widely advertised all three Lancers wines on television and in consumer and trade magazines (CX 359I).

108. Heublein was interested in developing different types of wines at the Lancers facilities (Tr. 4338).

109. New wines have been developed at the new winery facility in Portugal built by the joint venture in which Heublein participated (see Findings 56, 57, *supra*). Some of the experimental wines developed were Beijo Beijo, Jacare and Allegria (Tr. 4336–37). Heublein currently owns the Jacare label (Tr. 9999). Two line extensions for Lancers were developed and produced there, Lancers Vino Branco and Rubeo. Both are currently being imported into the United States (Tr. 4337–38). The joint venture makes Zazie wine for United Vintners (Tr. 8463).

110. Heublein imports and sells about 40,000 cases per year of the eight different types of burgundy wine in the Bouchard line and about 30,000 cases per year of the ten different Hungarian wines in the Monimpex line. These wines are sold through Heublein's Smirnoff Sales Company (Tr. 4429–30, 8829).

111. Heublein also imports limited quantities of Paraquita and Muscatel produced by the Fonseca family (Tr. 4334).

(f) Heublein's Continued Overall Post-Acquisition Growth

112. Heublein ranked 209th in terms of sales and 238th in terms of assets among the Fortune 500 for 1972 (CX 58L). By 1976, Heublein had risen to 176th position in terms of sales and 213th position in terms of assets (CX 369G).

113. In calendar year 1976, Heublein's growth in spirits was six times that of the industry as a whole. Heublein accounted for half of the total industry growth of 1 percent that year (Tr. 9260, 9262).

114. Heublein's fortunes took a downward turn in 1977. This, however, was due to an unusual convergence of external business factors such as downward trends in the wine industry and the alcoholic beverage industry and a severe economic financial crunch in Brazil (Tr. 9177–78). Heublein's chief executive officer believes that the difficulties Heublein experienced in 1977 are not symptomatic of a weakness in Heublein's business and the upward turn of sales in 1978 tends to bear this out (Tr. 9257; CX 543Z–10). Heublein's earnings per share rose in 1978 by 17 percent over 1977 (Tr. 9254). 1977 was the only year in which Heublein's earnings per share dropped (Tr. 9255). [27]

115. Heublein's Chairman and chief executive officer acknowledged that, except for 1977, Heublein has been classified as a growth company and a successful consumer package goods company (Tr. 9174).

116. By 1978, Heublein had grown in a few years from the fifth largest company in the United States spirits industry to the second largest. It was growing faster than any other spirits company with such a broad product line (CX 543F).

117. In 1978, Heublein's net sales were $1,577,114,000 and its net income was $56,529,000. Earnings per share were $2.66 (CX 543Z–10). As of June 30, 1978, Heublein's total assets were $861,388,000 (CX 543Z–19).

3. Heublein's Marketing Strength

118. Heublein's major brands and product lines are under the direction of product, merchandising and advertising managers. Heublein employs a full range of marketing techniques (CX 56Z–10).

119. Heublein's policy is to perform full marketing functions for products it handles rather than to act merely as sales agent (CX 46E, H, 65J).

120. In 1975, Heublein's Chairman identified two of four of Heublein's major strengths as (1) its marketing ability and (2) its unique position in the fastest-growing segments of the food and

alcoholic beverage business (CX 360F). Prior to the merger, it had the reputation of being a successful marketing company (Tr. 4958).

121. Shortly after it introduced canned, pre-mixed Club Cocktails, a new liquor category, Heublein reported "INSTANT SUCCESS"—that it had 90 percent distribution in its markets, a mark equalled only by a few brands of distilled spirits in the nation (CX 35B).

122. By 1967, Heublein's greatest single annual expenditure was $36,512,000 for advertising, merchandising and sales promotion. "The creative and effective use of the total marketing expenditure resulted in expanded activities at slightly lower overall costs." Heublein's advertising expenditure was used with multiple effect across its product line (CX 48M).

123. In the year ending June 30, 1968, Heublein's advertising expenditures were $8,562,000 (CX 24). [28]

124. Advertising, merchandising and sales promotional expenditures continued to constitute one of Heublein's largest expenditures, accounting for approximately $76,000,000 in fiscal year 1972, up from $68,000,000 the year before (CX 56Z–10). In 1962, the figure had been just under $25,000,000 and in 1966, it exceeded $35,000,000 (CX 47F).

125. Heublein used advertising effectively to increase sales (CX 38B, 46G, 47I, 48I, 50F, I, M, N, Q, R).

126. Heublein either set the trends or established itself as a leader in keeping pace with the trends. It marketed new products and capitalized on changing consumer tastes (CX 47D, 48E, F, J, 49G, H, I, K, M, 50E, F, I, J, M, Q).

127. Heublein also capitalized on the trend toward increased travel and became a leader with ship, rail and airline accounts (CX 44B, 48I, 50J).

128. In the year in which Heublein acquired United, it continued to emphasize marketing as it had in the past (CX 50E, F, J, M, Q).

129. Shortly after the acquisition, Heublein named Mr. Bonomo, described in Heublein's 1969 Annual Report as "an experienced marketing executive," as President of United (CX 50Q).

130. Heublein attributed many of its successes in the marketplace to "particularly effective marketing efforts" (CX 46E, 47G, 48I, L, M, 49K).

131. Heublein, as of the time of the merger, planned to continue in product categories where its marketing skills could assure success (CX 34G).

132. Heublein had expertise in mass advertising—advertising in great bulk, on a large or national scale (Tr. 9037).

133. Both Harveys and Lancers are high margin products with

high advertising to sales ratios (Tr. 3699; See Findings 696–97, 734–37, *infra*).

134. Heublein had a marketing services organization called the Venture Group that was available to do merchandising and sales promotional work at the retail level. The Venture Group handled the field introduction of new products, coordinated new products research and development, developed and executed marketing programs and handled sales to national accounts, including airlines and hotel chains (CX 359H; Tr. 8904–05, 3306–07). The Venture Group handled United's wines and Heublein's spirits (Tr. 3307). The Venture Group, for example, developed the name for T. J. Swann, a United product (Tr. 8582–83). [29]

135. Heublein is currently trying an arrangement whereby one sales group handles certain national accounts such as airlines, chain hotels and chain restaurants for both its spirits products and the products of United (Tr. 8905). Some of the national accounts are the Hilton Hotels, Holiday Inn and Pizza Hut (Tr. 3307).

136. As stated by Heublein's General Counsel, a "major amount" of Heublein's marketing expenditures is in unmeasured media, primarily merchandising material. With the caveat that these expenditures are difficult to ascertain, Heublein estimated that they amounted to approximately $10 million in each of fiscal years 1970 and 1971 (CX 332B).

137. As of the time of the merger, new product development and strong marketing were part of Heublein's business philosophy (CX 260).

138. In 1965, Heublein relied on its self-asserted "reputation in the industry as perhaps the most astute and successful merchandisers of alcoholic beverages" in its efforts to obtain the distribution and marketing rights for Jose Cuervo Tequila. Heublein asserted that its success in marketing other products had been a result of modern marketing concepts and aggressive selling programs (CX 178A).

139. Harveys Bristol Cream was stated by Heublein to be "the first quality Sherry to be advertised on U.S. television." By fiscal year 1967, advertising and promotion expenditures on Harveys Bristol Cream had been increased to the point that they were then greater than for all other sherries imported into this country (CX 48L).

140. Between its 1965/66 and 1970/71 fiscal years, Heublein's per case advertising expenditures for Lancers rose from $.57 to a projected $4.44 (CX 116B, I, W).

141. · Of brands of vodka utilizing outdoor media advertising in

the United States in 1976, Smirnoff lead the list with expenditures of $1,634,200 out of a total of $4,092,900 spent by vodka marketers for outdoor media. The second largest such advertiser spent $329,100 (CX 383F).

142. Of brands of vodka utilizing newspaper advertising in the United States in 1976, Smirnoff topped the list with expenditures of $832,900 out of a total of $2,912,954 spent by vodka marketers for newspaper advertising. The second largest such advertiser spent $582,357 (CX 383F).

143. Of brands of vodka utilizing magazine advertising in the United States in 1976, Smirnoff headed the list with expenditures of $4,067,353 out of a total of $6,147,804 spent [30]by vodka marketers for magazine advertising. The second largest such advertiser spent $896,245 (CX 383F).

144. In the United States in 1976, Smirnoff Vodka's $4,067,353 magazine advertising expenditures were larger than magazine advertising expenditures for any other brand of distilled spirits. Johnny Walker and Canadian Club ranked second and third respectively with expenditures of some $3,600,000 each. Heublein Cocktails ranked tenth with expenditures of $2,102,771 (CX 383M).

145. Of brands of prepared cocktails utilizing magazines, newspapers and outdoor media for advertising in the United States in 1976, Heublein prepared cocktails (including Hereford Cows and Kickers) had the largest advertising expenditures of any brands advertising in one or more of these media (CX 383L).

146. Of brands of tequila utilizing magazine advertising in the United States in 1976, Jose Cuervo topped the list with expenditures of $1,258,819 out of a total of $2,555,385 spent by tequila marketers for magazine advertising. The second largest such advertiser spent $369,833 (CX 383I).

147. Of brands of tequila utilizing outdoor media advertising in the United States in 1976, Jose Cuervo ranked second with expenditures of $410,700 out of a total of $1,298,700 spent by tequila marketers for outdoor media advertising. The largest such advertiser spent $451,900 (CX 383I).

148. *Advertising Age* reported that Heublein was the second largest advertiser among liquor companies and the 44th largest advertiser overall in 1970 (CX 57). In 1972, Heublein had risen to first rank among liquor companies in terms of advertising and 29th overall (CX 59). In 1976, Heublein was still ranked first among liquor companies and had risen to the 16th largest advertiser overall (CX 370).

While HUV assert that *Advertising Age* advertising data for

Heublein are incorrect (RR at 243–45), the relative ranking of companies is of probative value since uniform methods for ascertaining advertising expenditures would have been utilized for each company listed.

B. United Vintners

149. Prior to its acquisition by Heublein, United was an incorporated agricultural cooperative organized, existing and doing business under and by virtue of the laws of the State of California, the sole member of which was Allied. United was converted to a corporation in order to permit its acquisition by Vintners by means of a tax free exchange of shares (CX 9C–G). [31]

150. United, at the time of the acquisition, was a corporation organized, existing and doing business under and by virtue of the laws of the State of California and is such a corporation now (CX 221C; Heublein's Answer V, 13 (p. 9)).

151. United, at all times relevant herein, has had its principal office and place of business in San Francisco, California. At all times relevant herein, United has sold and shipped its products in interstate commerce and was engaged in commerce as "commerce" is defined in the Clayton Act and was engaged in or its business affected commerce as "commerce" is defined in the Federal Trade Commission Act (Heublein's Answer V, 13 (pp. 9–10)).

152. In the course of the acquisition transaction, a "new" Allied cooperative was formed to succeed to the rights and obligations of "old" Allied. The two cooperatives had substantially the same membership and the same rights and obligations with respect to its grower-suppliers (CX 9D, F; Tr. 2503–04). United, prior to the acquisition, held all of the production and marketing assets of "old" Allied and has continued to hold substantially all of those assets (Heublein's Answer V, 13 (pp. 9–10)).

153. United Vintners was formed by Louis Petri when his Petri Wine Company purchased the Italian Swiss Colony business in 1953 (Tr. 2371; CX 209C). United was owned by Louis Petri until 1959, when he sold the company to Allied for $24 million (Tr. 2372).

154. The brands of United which came with Allied's acquisition were Italian Swiss Colony, Petri, G&D (Gambarelli & Davito), Margo, Greystone, Mission Bell, Lejon and Hartley (Tr. 2372; CX 209B).

155. Among the facilities which Allied acquired by virtue of its 1959 purchase of United were wineries at Lodi, Clovis, and Asti. Allied had previously purchased (in 1951) the Escalon and Madera

plants from Louis Petri and had been operating them to produce wines for the Petri Wine Company (Tr. 2371–73; CX 209C).

156. From 1959 to 1968, United acquired additional brands and facilities. The Cella wineries at Reedley and Oakville and the Cella and Parma brands were acquired in 1961 for $1 million (Tr. 2385, 2388; CX 209B). In 1964, United acquired the Inglenook winery at Rutherford together with the Inglenook brand for approximately $1.1 million (Tr. 2385). At that time, Inglenook was well-known and had a reputation for high quality wines (Tr. 2394, 2677). John Martin, chairman of Heublein's executive committee, testified that he was informed that Inglenook was one of the two best Napa Valley premium wines (Tr. 4027). Inglenook sales went from 60,000 gallons in 1964, the year in which it was acquired by United, to 174,000 gallons in 1968 (Tr. 2395; CX 138C). [32]

157. Prior to the acquisition of a controlling interest in United by Heublein, United crushed the grapes delivered by Allied, processed the juice into wine and sold the resulting wine throughout the United States (Heublein's Answer V, 14 (pp. 10–11); CX 355; Tr. 2371).

158. In 1968, the year prior to the acquisition, United had eight wineries located throughout California and four bottling facilities in California. United also leased facilities in Chicago and Newark, New Jersey at which it bottled wine shipped from California (Tr. 2388–89; CX 55Z).

159. At the time of the acquisition, United sold wines principally under the Italian Swiss Colony, Inglenook, Petri, Lejon (sparkling wines and brandy), G&D, Margo and Bali Hai labels (CX 55Y, 209B). It also sold wines under a number of other labels including Tipo, Hartley (brandy), Bravo, Chateau Louis, Vai Bros., Marca Petri, Santa Fe, Arriba, Paree, Silver Satin, Cappella, Rhineskeller, Golden Spur, Hombre, Pombano, Parma, La Finesse, Padre, Jacques Bonet, Fior di California, Mission Bell and Greystone. In addition, United sold bulk wine to bottlers for bottling under United's franchised labels and under the bottlers' own private labels. In 1968, United sold approximately 4 million gallons of bulk wine to franchised bottlers for bottling under United's labels; it bottled bulk wine at its direct sales operations in Newark, Chicago and Los Angeles; and it sold bulk wine to other wineries (CX 22, 209C; RX 1206V; Tr. 2611, 3868–71, 9524–26).

160. In 1968, United produced wines of all types including dessert wines, table wines, sparkling wines, flavored wines, vermouth and brandy, as well as grape juice and wine vinegar. Most of the products were sold under brand names owned by United. It sold wines under

proprietary names such as Bali Hai and Silver Satin (CX 55Y). It sold wines at all consumption levels "from rare estate bottled vintages to popular priced varieties" (CX 50Q). All of these products were produced in United's wineries in California (CX 55Y).

161. In 1968, United sold its products to approximately 370 wholesale distributors (CX 55Y). In addition, United owned its own wholesale operations in the New York City, Cleveland, Southern California, Santa Barbara and Fresno areas, and parts of the Chicago area. These company-owned operations accounted for approximately 30 percent of United's sales (CX 55Y). United also sold its products to state and local agencies which control alcoholic beverage distribution in the so-called "control"[5] states (CX 55Y). [33]

162. Prior to the acquisition, United was a leading advertiser in the wine industry. United's advertising expenditures in its 1968 fiscal year for its Italian Swiss Colony brand alone were $3,657,000 (CX 231Z–63). This exceeded the 1971 advertising expenditures of all companies in the wine industry except Heublein (including Italian Swiss Colony) and Gallo (CX 231, 300L–M). This level of wine advertising expenditures was not reached by any other company until 1975, when Schenley for the first time exceeded it with an expenditure of $4,061,162 (CX 385M; see also CX 300K–M, 376L–O, 383L–O). B.C. Solari, United's President and Chief Executive prior to the acquisition and for two years thereafter, was "regarded [in a Heublein analysis] as one of the most astute merchandisers in the wine business today." He was said to be matched by only Ernest Gallo as a marketer of wine (CX 209D).

163. United's advertising expenditures in the 1960's for Italian Swiss Colony were:

1963/64	$3,701,000
1964/65	2,567,000
1965/66	2,702,000
1966/67	3,678,000
1967/68	3,657,000
1968/69	3,829,000
1969/70	4,110,000

(CX 231Z–63)

[5] "Control" states (Montana, Utah, Wyoming, Iowa, New Hampshire, Pennsylvania, West Virginia, Mississippi, and Montgomery County, Maryland) are those in which all wine sales are made under the direction of government officials (RPF 405 n. 1).

United was clearly one of the two top advertisers in the wine industry in each of the years listed above.[6]

164. United's financial condition as of 1968 was assessed by Paul Warnick, a CPA and partner (now retired) with Touche Ross and Company, the independent auditor for United and Allied. Mr. Warnick was responsible for the annual audits and certification of Allied's financial statements. He was a specialist in the field of agribusiness. Mr. Warnick summarized his assessment of United's financial condition as of August 31, 1968, the year prior to the acquisition, by stating that United "was a strong financial company" (Tr. 10879–80, 10883–84, 10926). [34]

165. United was consistently profitable from 1960 to 1968. Its proceeds varied principally with the variations in the market cost of grapes, as shown in the following table:

United Vintners, Inc.: Net Proceeds in Excess of Quoted Average Market Price for Grapes, 1960–1968 (FY's ending August 31)

1960	$2,796,922	(CX 547G)
1961	2,924,056	(CX 548G)
1962	1,673,736	(CX 549G)
1963	3,182,289	(CX 550G)
1964	6,659,591	(CX 551G)
1965	2,552,125	(CX 552G)
1966	5,118,805	(CX 553G)
1967	4,451,564	(CX 554G)
1968	3,301,356	(CX 555G)

For the 10-month period ending June 30, 1969, the figure was $1,359,438 (CX 556E).

166. United increased its dollar sales in each succeeding fiscal year during the 1960–1968 period. United's sales were:

1960	$51,089,141	(CX 547G)
1961	52,961,849	(CX 548G)
1962	65,663,911	(CX 549G)
1963	76,902,616	(CX 550G)
1964	80,144,988	(CX 551G)
1965	81,506,227	(CX 552G)
1966	86,231,076	(CX 553G)

[6] In 1970, the third largest advertiser, Schenley had advertising expenditures of $2,577,779.

1967	91,026,634	(CX 554G)
1968	96,009,189	(CX 555G)

United's sales for the 10-month 1969 fiscal "year" (ending June 30, 1969) were $95,461,271 which is the equivalent of $114,553,500 for a 12-month period (CX 556E). [35]

167. According to a Heublein submittal to the Federal Trade Commission (CX 328J, K, L, M), United's gallonage of wine shipments from 1960 to 1969 and its share of shipments of all wine produced in the United States for those years is as follows:

(in 000's)

	All Wine		Table Wine[7/]		Sparkling Wine		All Other Wine[8/]	
	Gallons	%	Gallons	%	Gallons	%	Gallons	%
1960	28,211	18.5	6,557	13.8			21,654	21.3
1961	33,467	21.0	8,463	16.7			25,004	23.8
1962	31,987	20.8	7,754	15.0			24,233	24.6
1963	37,628	23.3	10,230	18.2			27,398	27.1
1964	39,518	23.2	11,556	18.7			27,336	26.5
1965	41,495	23.9	12,708	19.5			28,102	27.5
1966	38,953	22.5	12,029	17.6	840	11.3	26,084	26.7
1967	40,830	22.2	13,838	18.1	1,142	13.0	25,850	26.2
1968	42,279	22.1	15,889	19.2	1,317	12.8	25,073	25.5
1969	46,048	21.8	20,388	21.0	2,418	17.6	23,242	23.2

7/ United's table wine figures include refreshment or pop wines. As found in Findings 438-48, infra, refreshment wines do not belong in the table wine submarket.

8/ As explained by Heublein (CX 328C), this consists primarily of dessert wines -- still wines over 14 percent alcohol by volume.

[36]168. Allied was optimistic in 1968 about the future of United. Robert McInturf, President and a founding member of Allied, testified that as of 1968 the outlook for sparkling and table wines was optimistic. The industry as a whole including United was experiencing increases in the sale of table wines (Tr. 2406). Buddy Iwata, Secretary of Allied and a member of Allied's executive committee since the 1950's was optimistic in 1968 about the future growth of United. Based upon the prospects for the wine industry and United's history of profitability, he was optimistic about United's future profitability as well (Tr. 2670–71, 2678–79).

169. In 1969, United shipped 19,450,100 gallons of table and refreshment wine or 16.2% of the total industry shipments of such wines. The third ranked firm in 1969 had less than one-fourth the table and refreshment wine shipments of United (CX 373Z–2).

170. United's 1969 table and refreshment wine shipments of 19,450,100 gallons had never been matched by any company other than Gallo and United itself through 1976 (CX 366Z–1).

171. United's 1968 table and refreshment wine shipments were 15.4 million gallons, or 15.6% of all such wine shipments (CX 373Y). [37]

336-345 O - 81 - 28

172. While United, sometime after September 1970, took steps to increase its refreshment wine business (Tr. 7778, 7796-97), it had already, prior to the merger, been able to capture a significant share of this newly developing market, as demonstrated by the following table:

Refreshment Wine Shipments
(Derived from RX 15, 27)

	1967		1968		1969[9/]	
	Gallons (000s)	%	Gallons (000s)	%	Gallons (000s)	%
Gallo	1563	56.20	3354	66.03	8321	58.30
United	1063	38.26	1752	32.92	5562	38.97
Robinson-Lloyds	75	2.7	97	1.82	154	1.08
Monsieur Henri	25	.9	55	1.03	110	.77
Mogen David	24	.86	26	.48	38	.26
Monarch	24	.86	32	.6	54	.38
Leonard Kreusch	4	.14	4	.07	6	.04
Gibson			1	.02	23	.16
Guild					3	.02

9/ 1969 figures are included since the post merger activities reflecting an increase in effort and "updating" of United's facilities to produce refreshment wines were not instituted until after September 1970.

[38]173. United, therefore, prior to the merger was demonstrably capable of competing in a newly growing market area and of capturing a major share of that market. While second to Gallo, it was clearly a dominant company in comparison with any other competitor to the point of outselling the number three competitor many times over.

174. United's wine was produced by United in its own wineries (Tr. 9327, 10710–12). United's 1969 shipments were made from grapes crushed in 1968 or earlier (Tr. 7894–95).

175. In the early 1960's, Allied learned from the sales trends of United, from reports made by United's management at board meetings and from Wine Institute industry statistics that table wines were increasing and dessert wines were decreasing in importance (Tr. 2585, 10712–13).

176. As a result of this awareness, Allied took steps to prepare United for the increased production of table wines. In 1962, the crushing capacity at its main plant at Madera, California was doubled and the storage capacity was increased through the addition of many 600,000 gallon stainless steel tanks. Refrigerated production equipment was also added at that time. The improvements in 1962 were valued at over $3 million (Tr. 2388, 2620, 2636–37, 10714–15, 10718; CX 549S). Additional improvements were made at Madera in 1964 when a new bottling plant and warehouse for cased wine were added. Improvements at Madera in 1964 were valued at over $2.1 million (Tr. 2637, 10727–28; CX 483A–B, 551S).

177. The Escalon, California winery of United was converted from a dessert to a table wine winery prior to the acquisition (Tr. 2619–20). As part of its ongoing program of conversion to table wines, United carried out a three-year expansion program at Escalon which added cooperage and refrigeration (Tr. 10728; CX 484B). In 1964, one million gallons of new tanks were added at Escalon (Tr. 10729–30; CX 484B). The expenditures for improvement at Escalon in the 1964–1967 period were as follows:

	1964	$ 188,486	(CX 551S)
	1965	680,545	(CX 552R)
	1966	503,666	(CX 553R)
	1967	279,205	(CX 554R)
(1964–67)	Total	$1,651,902	

178. By 1968, the annual capacity of the Escalon plant had been increased to 13,562,000 gallons, which would have ranked that one

winery alone as the 14th largest company in capacity in 1976 (CX 55Z, 366Z–10). [39]

179. In 1964, United purchased the prestigious Inglenook winery, which produced table wines exclusively. It then added a bottling plant to Inglenook's Rutherford winery. United's Oakville winery, which it had purchased in 1961, was then improved and put into service in 1966 to produce table wines for Inglenook (Tr. 2388, 10728–29; CX 484B). The Oakville winery today produces Inglenook table wines which are bottled at the bottling plant at Rutherford (Tr. 9333, 9793).

180. The Asti winery of United was largely a producer of table wines (Tr. 2636). From 1962 to 1968, constant improvements were being made at Asti. The expenditures for improvements at Asti were:

	1962	$ 318,929	(CX 549S)
	1963	277,454	(CX 550R)
	1964	115,939	(CX 551S)
	1965	371,003	(CX 552R)
	1966	382,941	(CX 553R)
	1967	233,223	(CX 554R)
	1968	206,079	(CX 555P)
(1962–68)	Total	$1,905,668	

181. United, prior to the acquisition, had plans for a new table wine brand, Napa Valley Winegrowers. It was expected that the brand would sell 1.5–2.5 million cases within five years of its introduction (CX 228A, B).

182. Prior to 1968, in anticipation of the increased importance of table wines, Allied had initiated a program of acquiring grapes which would be suitable for table wines. It had held discussions with its members to encourage the planting of the grape varieties which would be needed to produce table wines and had worked on a grape breeding program to develop grape varieties which would lend themselves to the production of table wines (Tr. 2419–21, 10714).

183. Grape Factors, which in the early 1960's supplied grapes needed by United which were not available from Allied's members, was no longer needed after 1964 (Tr. 2628).

184. United's shipments of branded products ranked it first or second in every wine product market and submarket in every year (except sparkling wines in 1968, when United ranked third) from 1967 to 1972 (CX 373).

185. Italian Swiss Colony was one of the top brands in the industry. In United's fiscal year 1969/1970, Italian Swiss Colony

shipments of approximately 12 million gallons would have ranked that single brand as the second ranking company in the industry (CX 231C, 373H). Italian Swiss Colony was the second largest brand in the industry [40]in September 1970 (Tr. 7778, 7986). Italian Swiss Colony was sold nationwide in the preacquisition period and had been a national brand as early as 1953 (Tr. 2207–08, 2392–93).

186. Allied, as of 1968, had completed paying Louis Petri for United Vintners. Payment of the purchase price of $24 million was completed a year and a half ahead of schedule (Tr. 2433–34, 2686).

187. United's sales since the acquisition have continued to increase at a healthy pace. United's sales of approximately $96 million in 1968 have increased to _____ in 1978 (CX 555G, 565F *in camera*). See *In Camera* Addendum.

188. United's total shipments of wine have also increased since the acquisition—from approximately 38 million gallons in 1968 to approximately 56 million gallons in 1976 (CX 373D; RX 1257).

189. According to Heublein's 1976 Annual Report, "With new products, new values and aggressive marketing both Beaulieu Vineyard and United Vintners had record years. For the fourth consecutive year, U.V. increased its share of the U.S. wine business" (CX 361F). The Heublein 1978 Annual Report also reported that United "increased its market share and had the second most profitable year in its history" (CX 543F).

190. At the time of the acquisition, United had products in virtually all product categories. In table wines, United's brands included Inglenook, Italian Swiss Colony, Petri, and G&D. It also had Bali Hai, a refreshment wine (CX 472C; Tr. 2393–97). In dessert wines, United had Italian Swiss Colony, Inglenook, Petri and Lejon (for vermouth) (Tr. 2393–94; CX 472C). In sparkling wines, United had Lejon and Jacques Bonet (Tr. 7900; CX 472C).

191. Soon after the acquisition, there was a shift in emphasis among products. Richard Oster, who became United's President in September 1970, made an effort to emphasize refreshment wines (Tr. 7778, 7796–97). The major priority in United's marketing was to shift the emphasis to Annie Green Springs, a refreshment wine (Tr. 3308–09).

192. During the same time period after the acquisition, some of the existing brands and items were discontinued (Tr. 7783).

193. In June 1972, Oster informed Allied's members that United was in the enviable position of being the only true full-line wine marketer in the United States (Tr. 8001). He also informed Heublein that United was the "strong number two factor" in the United States wine industry (Tr. 8000). [41]

194. After the acquisition, United introduced a number of new brands. In 1972, it introduced the Annie Green Springs brand of refreshment wines (CX 53G, 247D), and sold 1,000,000 cases in the first six months after national introduction (CX 371). By United's fiscal year 1974, the brand was selling 3 million cases per year and by 1975, it was selling 4 million cases per year. It sold 10 million cases in the three years following its introduction (CX 359L, 360N; Tr. 9838–39).

195. In fiscal year 1974, United introduced the T.J. Swann brand of refreshment wines (CX 359L). By 1975, T.J. Swann sales were approximately 2 million cases per year (Tr. 9839). By 1977, the T.J. Swann case volume was _____ cases (CX 585B *in camera*). T.J. Swann was a highly profitable brand for United. Its product line earnings were expected to be _____ in 1977 (CX 585Z–14 *in camera*). Though marketed by United, this brand is owned by Heublein (Tr. 2511; CX 358C). See *In Camera* Addendum.

196. Sangrole was a sangria-type product introduced by United during Richard Oster's presidency (Tr. 7946). Mr. Oster was President of United until September 1973 (Tr. 7778). The introduction of Sangrole was a success (Tr. 7946). Sangrole continued to be sold in 1978 (CX 585A, B).

197. Bali Hai was a refreshment wine originally introduced in 1963 (Tr. 7908, 7913). Subsequent to the acquisition, approximately in 1971, Bali Hai was repackaged and renewed activity was placed behind it. In that year, $1 million was spent in advertising Bali Hai (Tr. 3707–08).

198. United markets Jacare, a line of three table wines introduced in United's 1977 fiscal year (Tr. 8509; CX 585Z–35).

199. United markets Zazie, a refreshment wine. Zazie is imported from Portugal where it is made at the Heublein-Fonseca joint venture winery (Tr. 8463, 8509, 9842). Although marketed by United, Zazie is not imported by it (CX 446).

200. Italian Swiss Colony was the largest brand of United at the time of the acquisition (Tr. 2390). Its name was changed to Colony, though the wines are still called Italian Swiss Colony (CX 536F; Tr. 8429). Italian Swiss Colony (or Colony) is still one of the basic brands of United and is the largest in volume (Tr. 9502; CX 585Z–16 thru Z–22). A highly successful line of varietal wines has been added under the Colony label (CX 361D). [42]

201. Petri also remains one of the basic brands of United (Tr. 9502; CX 34C). Lejon and Jacques Bonet, the brands of sparkling wine at the time of the acquisition, continued to be emphasized

thereafter (Tr. 7900). They remain the basic sparkling wine brands of United today (Tr. 9502).

202. Inglenook is one of the fastest growing major brands of California wine and, according to Heublein's 1977 Annual Report, in fiscal year 1977 had a case volume increase of more than 30 percent. Inglenook, in fiscal 1978, became the fastest growing major brand in the industry with a growth of almost 50 percent and sales of almost 4 million cases (Heublein's 1978 Annual Report, CX 543N). It was estimated by United (two months before the end of United's fiscal year) to have shipments of _____ cases in 1978, up from actual shipments of _____ in 1977 (CX 585C *in camera*). See *In Camera* Addendum.

203. Inglenook's Navalle line was successfully introduced by United in 1971 (Tr. 8462). In fiscal year 1978, Navalle shipments were 3.4 to 3.5 million cases or 85–90 percent of all Inglenook shipments (Tr. 8525–26). The Navalle product line earnings were estimated (two months before end of fiscal year 1978) to be _____ on sales estimated at _____ in fiscal year 1978 (CX 585G *in camera*). The comparable figures for fiscal year 1977 were product line earnings of _____ on sales of _____ increases of over ____ percent from the previous year (CX 585Z–12, Z–13 *in camera*). See *In Camera* Addendum.

204. Heublein (through United and under United brands) produces and markets wines of all types, including table wines, dessert wines, sparkling wines and flavored wines including vermouth. Italian Swiss Colony and Colony are two of United's most popular brands and are distributed throughout the United States. Inglenook wines, marketed in the Cask, Estate, Vintage and Navalle lines, are distributed nationally (CX 358C). Proprietary names are used for refreshment wines such as Annie Green Springs, T. J. Swann and Jacare (CX 358C; Tr. 9824).

205. United has distribution in all 50 leading metropolitan markets and has approximately 435 distributors (Tr. 9621, 9872).

206. In the two largest markets for wine in the United States, New York City and Los Angeles, United owns its own wholesale distribution operation (Tr. 9718–19; CX 533A). United's wholly-owned wholesale operation in New Jersey serves all of New Jersey as well as New York City (Tr. 9643–44). United's Southern California wholly-owned wholesale operation serves all of Southern California (CX 533). United's own wholesale operations in addition [43]serve three of the top 15 markets for wine (CX 533A–C). The six markets of the top 15 served by United's owned distributors accounted for 21.5%

of wine sales in 1976 (CX 379U). These distribution operations sell wines only (Tr. 9718–19).

207. In order for a wine company to operate its own directly-owned distribution system, it must have a strong brand and a large scale of operations (Tr. 3312). United has 145 salesmen in its Southern California distributor and about 90 in the New York/New Jersey distributor (Tr. 9928).

208. Despite the fact that United's own wholesale distribution system is operating at a loss, it constitutes an advantage to the overall winery operations (Tr. 9720–23).

209. United's wineries are as follows:

Location	Area (Sq. Ft.)	Function
Asti	363,200	Winery, bottling
Clovis	271,400	Winery, brandy production
Escalon	144,700	Winery
Lodi	115,700	Winery, brandy production
Madera	775,800	Winery, bottling
Oakville	50,000	Winery
Reedley	221,500	Winery, bottling
Rutherford	230,576	Wineries, bottling (CX 358H)

210. Capacities and production as of the time of the acquisition were:

Location	Annual Capacity	Production (Year ending Aug. 31, 1968)
Asti (winery)	9,269,000 gal.	4,115,522 gal.
(bottling)	1,300,000 cases	884,360 cases
Clovis (winery)	15,216,000 gal.	6,514,292 gal.
Escalon (winery)	13,562,000 gal.	8,096,519 gal.
Lodi (winery)	4,227,000 gal.	3,738,680 gal.
Madera (winery)	25,015,000 gal.	12,782,157 gal.
(bottling)	9,000,000 cases	8,098,580 cases
Oakville (winery)	1,532,000 gal.	991,994 gal.
Reedley (winery)	11,770,000 gal.	6,085,259 gal.
(bottling)	1,000,000 cases	271,064 cases

Location	Annual Capacity	Production (Year ending Aug. 31, 1968)
Rutherford (winery)	302,000 gal.	
(bottling)	180,000 cases	60,062 cases
Total Annual Capacity:	80,893,000 Gal.	
Total 1968 Production:	42,224,423 Gal.	

(CX 55Z) [44]

211. Madera is United's largest winery and has been its main plant since before the acquisition (CX 55Z; Tr. 2388, 10,717). Its capacity was doubled during the 1960's and its new facilities were used in producing table wine (Tr. 2637–38). The glass bottle plant supplying United's bottle requirements is located at this winery site (Tr. 9219). Annie Green Springs and T. J. Swann are produced at Madera, and it is the primary facility for Italian Swiss Colony table wines (Tr. 9901). Mr. Stuart Watson, Chairman of the Board and chief executive officer of Heublein, has attested that the Madera plant is essential to the competitive viability of United (Tr. 9333).

212. Asti is the site of the Italian Swiss Colony visitor facility. This is an important element in the image and advertising of the Italian Swiss Colony brand, which bears the name of the original settlement (CX 443A–B). Jacare is produced at Asti (Tr. 9824). It is one of the wineries used for the bottling of Inglenook wines (Tr. 9793). More than $1.5 million were spent in improving Asti between 1967 and 1972 (Tr. 10002–03). Mr. Watson has testified that Asti is essential to the competitive viability of United (Tr. 9333).

213. Rutherford is the showplace winery of United (Tr. 9333). Rutherford is located in the well-known Napa Valley and thereby provides a prestigious address for Inglenook (Tr. 4087). It is not an operating winery, but does bottle Inglenook wines and is the site of the Inglenook testing room (Tr. 9333, 9793). According to Mr. Watson, Rutherford is significant to the competitive viability of United (Tr. 9333).

214. Oakville is a producing winery for Inglenook (Tr. 9333). The crushing of grapes and wine production for Inglenook wines is done at Oakville and the wines are then sent to Rutherford for bottling and aging (Tr. 10729). Cooperage was increased at Oakville in the mid to late 1960's (Tr. 10729). Mr. Watson agrees that Oakville is essential to the competitive viability of United (Tr. 9333).

215. Escalon is a major winery of United at which "premium"

wines are produced. Wines made at Escalon are shipped to Asti for bottling (Tr. 9885; CX 55Z). Inglenook Navalle is the primary brand produced at Escalon. Wines used in the Italian Swiss Colony varietal table wines are also produced at Escalon (Tr. 9945-47). Escalon was converted in the 1960's from dessert wine to table wine production (Tr. 2619).

216. The Reedley plant produces primarily Italian Swiss Colony wines. It is also used for the production of the Petri brand (Tr. 9947) and has a bottling facility (CX 358H). [45]

217. In 1968, glass supply problems and price increases prompted United to decide to build its own plant for production of glass bottles to be located adjacent to the Madera winery. In a management report presented to United's Board of Directors, the President of United reported on the proposed glass plant, that: "Plant capacity should be 13,000,000 cases to include Chicago bottling, and close to 15,000,000 to also include Newark. The estimated saving on the 13,000,000 case plant would be $1,958,000 per year. With a yearly write-off of $702,000, the cash flow would be $2,660,000 for a five year payoff. It would take four years to recover the cash outlay" (RX 1261B). The total cost to United thus would have been $10,600,000.

218. United was able to secure a $3 million long-term loan commitment from the Small Business Administration to finance construction of the glass plant (Tr. 2423, 2681, 9305), and an additional loan commitment from a bank (Tr. 2681). United planned to build the glass plant adjacent to the Madera Winery (CX 259B). Plans to build the glass plant were suspended because of the acquisition negotiations with Heublein (Tr. 2423, 2681). United would have built the glass plant even if the acquisition had not occurred (Tr. 2425, 2681; CX 259B).

219. The glass plant, the Madera Glass Company, was built in 1969, after the merger, as a joint venture with the Indian Head Glass Company owning 51 percent and United owning 49 percent. United is committed to taking the entire output of the plant (CX 557G). United enjoys a 15 percent cost saving on bottles and has earned a profit from the joint venture (CX 563F, 564F, 565F).

220. United's total initial investment in the Madera Glass Company was $1,960,000 (CX 557G). The commitment for a $3 million loan from the Small Business Administration was also utilized (Tr. 9305). United's total investment in the company reached a high of $4.4 million in 1977 (CX 565D). Heublein's participation in financing the Madera Glass Company was the guarantee of long-term loans of $5 million from Aetna Insurance Company, $3 million from Wells-Fargo, $2 million from the Bank of America, and $1

million from the Crocker-Citizens National Bank (Tr. 9220–23). The Madera Glass Company supplies 90 percent of Heublein's requirements of domestic wine bottles (CX 358D).

221. Subsequent to the acquisition, United purchased the land and winery of the Oakville Vineyards. This is adjacent to United's Oakville Winery (Tr. 9887, 9978–79). [46]

222. United had been able prior to the acquisition to borrow money at reasonable interest rates (Tr. 2426–27, 10,914).[10] As of August 31, 1968, United had long-term debts of only $7,061,908 and members' equity amounted to $25,319,318 (CX 555E). The three long-term loans which comprised over 95 percent of the long-term debt were at interest rates of 5 1/4 percent, 1/2 percent over prime, and interest-free, respectively (CX 555H–I).

C. Allied Grape Growers

223. Allied Grape Growers ("Allied"), is an incorporated agricultural cooperative association, organized, existing and doing business under and by virtue of the law of the State of California, with its principal office and place of business in Fresno, California (Heublein's Answer IV, 10 (p. 8)).

224. Prior to Heublein's acquisition of a controlling interest in United, Allied was in the business of acquiring grapes and supplying them to United for the production of wine (CX 55X; Heublein's Answer IV, 10 (p. 8)).

225. Allied was started in 1951 as a farmers cooperative with 230 members (Tr. 2366–67, 2381). It was formed to supply grapes to be produced into wine and sold by the Petri Wine Company (Tr. 2368). The wines were produced in the Escalon and Madera, California, wineries, which were purchased by Allied in 1951 from Louis Petri (Tr. 2368, 2373). The brands and facilities of United Vintners were purchased by Allied from Petri in 1959 (Tr. 2369).

226. Allied's members entered into three-year contracts for the sale of their grapes to Allied, which agrees to sign up a specified tonnage of its members' grapes during that period. The membership of Allied has changed substantially since the acquisition. Many growers who were members of Allied prior to the merger have withdrawn and a number of growers who were not members in 1968 have joined (RX 1018, 1019, 1020, 1026, 1027; Tr. 2374–75).

227. After it acquired United, Allied entered into agreements with its members for grapes to be delivered to United (Tr. 2369, 2375). The money generated (after expenses) from the sale of wine by

[10] There is record reference (RX 1195) to a particular financial institution refusing financing. The circumstances and nature of the financing, however, were not developed on the record.

United was paid to the members of Allied following the delivery season. The amount of money generated (after expenses) from the sale of wine above the market value of the grapes delivered is called "excess over [47]market" and represents the growers' earnings from United (Tr. 2369; CX 555G). The amount payable to each individual member was based upon the market value of the grapes he delivered (Tr. 2377). Out of the amount payable to the grower a certain percentage was retained by Allied (called a "retain"). The accumulated retains from the growers constituted the capital of Allied. The retains were paid back to the grower over a six-year period (Tr. 2376).

228. The average market price for grapes was based upon reports of the Federal-State Market News Service, a government agency which publishes the prices paid for grapes by wineries according to grape variety and growing area (Tr. 2378).

229. The average market price for grapes was $44.19/ton for the 1960–1968 period (RX 1219).

230. During the period 1959–1968, the weighted average market price for grapes delivered to United was approximately $50 per ton (Tr. 2409). The weighted average return to the grower members over the market value was $10 per ton (Tr. 2408, 2715).

231. Allied's members, in addition to the average market price for grapes, received their pro rata share of the excess over average market price for grapes. The excess over average market price was generated by United from the sale of wine and represented the earnings of United (Tr. 2377, 2379).

232. Money retained in a particular year, after a time lag of about a year, was paid back in quarterly installments over a six-year period (Tr. 2376, 2541–42). The grower built up his retains for six years and thereafter would, in quarterly installments, receive money from the retain fund as well as payment of what was not retained (Tr. 2376).

233. The average retain over the 1959–1968 period was $10.50/ton. The average net proceeds in excess of quoted average market price for grapes was about $10/ton for the 1959–1968 period (Tr. 2374).[11] The $10/ton average for the return above the $44.19/ton average market price is a return of about 23 percent. The $10.50/ton retain is [48]approximately 19 percent of the $54.07/ton ($44.19 + $9.88) average total price per ton of grapes.[12]

[11] There was an average 15-month waiting period for grape payments. The grower would be receiving the proceeds from his previous year's crop during this period. Crop loans were also available to growers from Allied, if needed (Tr. 2560).

[12] Average return over market for the 1960–1968 period calculated from United's financial statements from 1960–1968 (Pages G from CX 547–55; RX 1219).

234. The retain account represented the growers' equity capital in United (Tr. 2385, 10895, 10919; RX 1015B; see, *e.g.,* CX 553F).

235. The earnings of United or return over market and the market price were paid to the grower (less the retain) beginning about one year after the crop was delivered (Tr. 2545, 2557–58; see also, *e.g.,* CX 553M).

236. A change in the tax law in 1966, whereunder the grower would have had to pay taxes on retains kept by United, caused a change in form of United's retain fund. With the change (prior to the 1968 fiscal year) in United's retain fund from a "revolving fund" to a "capital fund", the growers' equity was considered permanent, not revolving capital. The financial consequence to the individual member was essentially the same, but retains were not considered to be paid in by members for the current year and paid out by United for the crop six years before. Instead, the grower was considered to have a permanent investment and share in United which was maintained by payments from or to the member depending upon whether his proportion of the annual crop increased or decreased (RX 1014A–E, 1015Z–6; Tr. 10,943–44).

237. United's retains account had grown to $25,319,318 by 1968 (CX 554E, F, 555E).

238. During the 1959–1968 period, Allied had paid Louis Petri $24 million for United. It did so using money generated from the retains of $10.50/ton. The return over average market price for grapes averaged $10/ton over the same period (Tr. 2374, 2675–76). The payment for United, therefore, reflected the profits of United (Tr. 2374, 2674). While these profits may be said to have been held back from the growers, the growers received the full average market price for their grapes and in addition acquired a share in the increasingly valuable assets of United.

239. The average market price for grapes delivered by Allied's members prior to the acquisition (1960–1968) was $44.19 and the average market price for grapes delivered by Allied's members after the acquisition (1969–1977) was $90.64 (RX 1219). [49]

240. Allied recognized that the capital requirements for United would increase and so changed the form of the retain fund from a revolving to a capital fund. The change facilitated an increase in the capital investment in United (Tr. 10,943–44; RX 1014A–E, 1015D, E, Z–9, Z–10). United's capital requirements were determined by its board of directors and funds were retained in or paid out of the capital fund accordingly (RX 1015Z–8, 1020I).

241. By 1968, the membership of Allied had grown to 1,600 from the original 230 in 1951. The grapes signed up by Allied had grown

from 50,000 tons in 1951 to 410,525 in 1968 (Tr. 2381). In 1968, and for some four years prior thereto, there was a waiting list of additional grapes which the growers wanted to deliver through Allied. In 1968 or a year or two before, there were 100,000 tons on the waiting list (Tr. 2387, 2537).

242. After the merger, United continued to crush the grapes delivered by Allied's members and produce wine (Heublein's Answer V, 15 (p. 11)). Grapes were delivered to United by Allied pursuant to a long-term supply contract that had been entered into coincident with the merger (CX 221).

As recited in the Preliminary Statement, *supra,* p. 7, that long-term supply contract was declared invalid in a private suit, *Allied Grape Growers* v. *Heublein, Inc.,* Civ. No. C-75-0456 (D. Cal., filed July 21, 1978), and Allied subsequently sold its entire 18 percent interest in Vintners to Heublein.

D. Heublein Allied Vintners

243. Heublein Allied Vintners, Inc. ("Vintners") was a corporation organized on September 24, 1968, for the purpose of the acquisition of United by Heublein. Vintners' sole asset was 100 percent of the stock of United (Answer of Heublein Allied Vintners to Amended Complaint, VII pp. 2-3). Vintners was a holding company (CX 328D). Heublein had an 82 percent interest in Vintners and Allied had an 18 percent interest in Vintners (CX 211, 328F, H).

As recited in the Preliminary Statement, *supra,* p. 9, after Allied sold its 18 percent interest in Vintners to Heublein in 1978, Vintners on November 9, 1978, was merged into Heublein and ceased to exist.

III. EVENTS LEADING UP TO THE ACQUISITION

244. Mr. Louis Gomberg, a wine industry consultant and merger broker (Tr. 1402, 1410-11), by letter dated September 28, 1967, first called to the attention of Heublein (through its Chairman, John Martin) the possibility that United might be a candidate for acquisition (Tr. 1420, 4009; RX 1130). [50]

245. Mr. Gomberg had approached Mr. Bruno C. Solari, President of United, about a possible acquisition. Mr. Solari expressed a willingness to listen to any offer, but took no initiative in seeking anyone to acquire United (Tr. 1421-26).

246. Mr. Martin met with Mr. Gomberg on the West Coast in the fall of 1967, and they discussed various acquisition candidates (Tr. 4485, 4491-92). Mr. E. W. Kelley, Executive Vice President of Heublein, was then assigned to find out from Mr. Gomberg whether

any of those wineries would be interested in talking to Heublein. Mr. Gomberg said that he would talk to United and see if they were interested (Tr. 4493).

247. Later in the fall of 1967, Mr. Bruno C. Solari went to New York for purposes unrelated to consideration of a merger (Tr. 4718–19). While he was in New York, a representative of Heublein called to set up a meeting with him (Tr. 4716). Mr. Watson and Mr. Martin came to meet with Mr. Solari in New York and they told him they were interested in the possibility of buying United (Tr. 4008–09, 4720).

248. In December 1967 or January or February 1968, key executives of Heublein agreed that they wanted to look into the United matter and decided that Mr. Kelley should pursue it (Tr. 4500–02).

249. In March 1968, a contingent from United including Mr. Solari went to Hartford to discuss the matter with Heublein (Tr. 4566, 4568–69, 4721). There, Heublein presented its general plan of acquisition for the United representatives to report back to their board of directors (Tr. 4867). Heublein proposed a purchase price of about $38 or $38.5 million (Tr. 4868–69).

250. Until Mr. Solari told the Allied and United Boards of Directors (actually the same board) early in 1968 of Heublein's interest in acquiring United, there had been no interest on the part of either board or either company in selling out. Neither board had approached any company with respect to the possibility of selling United and no one had been authorized to explore the sale of United to another company (Tr. 2430–34, 2682–85).[13] [51]

251. Mr. Kelley met with Mr. Solari and Mr. Gomberg in California in April 1968 to discuss a possible Heublein-United merger (Tr. 4496). Shortly after that meeting, Mr. Kelley met in San Francisco with Mr. Solari and his associates to discuss the matter (Tr. 4573).

252. After obtaining information on United, Mr. Kelley returned to Hartford, where Heublein decided to pursue the possible acquisition further. Inasmuch as Heublein also had other opportunities, it was decided to make a study of the alternative means of entering the wine industry. McKinsey and Company was hired to do a study of four or five ways to enter the wine industry and to evaluate the merits of the United approach (Tr. 4512–13).

[13] Mr. Solari, who was President of United at the time of the merger and continued in that position under Heublein, recalled meetings with Welch Grape Juice in the middle 1960's to "explore the acquisition or a merger or how could the two companies do better by working together than working apart" (Tr. 4723). Welch withdrew from the talks (Tr. 4724). Mr. Solari, however, confirmed the testimony of other United and Allied officials that no one on the Allied board asked him to initiate any talks or explorations as to the sale of United (Tr. 4722).

253. Two to four weeks after it was commissioned, the McKinsey study of theoretical alternatives for entering the wine industry (RX 1212A-Z-15) was presented to Heublein (Tr. 4533). It was presented at a meeting on May 13, 1968, which was attended by a group of Heublein executives including Mr. Hart, Chairman of the Board and Mr. Watson (Tr. 4531). The four inside members of Heublein's Executive Committee were presented with the McKinsey report as a group (Tr. 4613).

254. Over the course of the negotiations regarding the acquisition of United, Heublein increased the price it was willing to pay (Tr. 2442).

255. During those negotiations, presentations were made by representatives of Heublein to the Boards of Heublein and Allied. Presentations were made by Stuart Watson, President, Edward Kelley, Executive Vice President, Ralph Hart, Chairman of the Board and John Martin, Chairman of the Executive Committee of Heublein. Other Heublein officials were also present. In addition, there were district meetings with members of Allied to persuade them to vote in favor of the merger. A total of 33 district meetings (three sets of meetings at each of 11 districts) were held at which Heublein representatives were present or at which Allied and United board members made the presentations prepared by Heublein (Tr. 2445-48, 2461-79).

256. Heublein represented to Allied that it was very knowledgeable in the wine business and that it had made a thorough study of the California wine business (Tr. 2468). Mr. Kelley represented to Allied in the fall of 1968 that Heublein had studied the domestic wine business for two or three years (Tr. 2777). Heublein presented itself to Allied as a good marketer (Tr. 2460-62, 2476-78, 2688-89, 2697-2700, 2773, 2776; CX 263, 264, 267). [52]

257. Heublein utilized charts and other visual and verbal presentations to demonstrate Heublein's growth as detailed in Findings 44-74, *supra* (CX 263, 264, 265, 266, 267; Tr. 2473, 2476-77, 2697-2700).

258. Heublein representatives pointed out that Heublein had a wide distribution system and that Heublein's and United's products were compatible so that the distribution of United's wines could be enhanced by using Heublein's distributors; Smirnoff vodka was cited by Heublein as a product which could be used to gain better distribution for United's wines (Tr. 2464-68, 2487). By having Lancers wine and Smirnoff vodka along with United's wine, the two companies could both increase the distribution of their products and both could use each other's warehouses (Tr. 2690-91, 2696).

259. Representations were made that the merger would result in

increased efficiency with the advertising dollar because of the joint effort (Tr. 2508–09, 2692–93).

260. It was also pointed out that the combination of Heublein with United could result in getting greater shelf space at the retail level (Tr. 2695).

261. Prior to the acquisition, there were discussions between Heublein and United with respect to consolidation of distributors and marketing efforts (Tr. 8926–27; CX 422).

262. On the basis of the foregoing findings under this heading as well as the description of United prior to the merger, it is concluded that United and Allied did not enter the merger arrangement because of any inability to continue in business on their own; that they did not initiate any steps seeking to be acquired, but that, when presented with a merger offer which appeared to be to their advantage, they accepted such an offer.

IV. THE ACQUISITION

263. A "Plan and Agreement of Merger" was entered into as of August 31, 1968 among Allied, Vintners, Heublein and Connecticut Vintners, Inc.[14] That agreement was executed on September 26, 1968 (CX 211A, O).

264. The agreement provided that Heublein would acquire a controlling interest in United (CX 55D–F, 211A–C). Prior to the acquisition, United had been a cooperative whose sole member was Allied (CX 211D). United was the production and marketing arm of Allied (CX 55X). [53]

265. The acquisition, effectuated on February 21, 1969, gave Heublein a controlling interest in United (CX 5, 55D–F).

266. Heublein, as consideration for the interest it acquired in United, gave shares of Heublein common stock valued at approximately $7,521,000, Series A Heublein preferred stock valued at approximately $20,319,000, and Heublein Series B preferred stock valued at approximately $5,000,000. The total value of the shares paid by Heublein to members of Allied and former members of Allied in exchange for their interest in United was valued at approximately $33 million (CX 136D).

267. Prior to the acquisition, United had been converted from a cooperative association to a corporation whose sole owner was Allied (CX 211I, 328D–H). As the result of a complex reorganization, United became a wholly-owned subsidiary of Vintners, a company organized

[14] Connecticut Vintners, Inc. was a wholly-owned subsidiary of Heublein which was merged into Vintners as one of the steps in effectuating the acquisition (CX 211).

for purposes of the acquisition (CX 328D–H, 211A–C). Also as a result of the reorganization, Heublein acquired an 82 percent interest in Vintners and Allied acquired an 18 percent interest in Vintners (CX 328D–H, 211A–C).

268. Since the merger, United has been operated as a subsidiary of Heublein (CX 136E).

269. As a condition precedent to the merger agreement, Allied, Heublein, Vintners and United entered into a supply contract, which also was executed on February 21, 1969, the date of the merger (CX 211M, 321Q). The supply contract provided that Allied would act as the supplier of all of United's grape requirements for 20 years, renewable for six additional ten-year terms at the option of Allied (CX 221D–E). It also provided that Allied was entitled to 20 percent of United's pretax profits and to designate eight members of United's 20 member board of directors (CX 221 O).

270. The supply contract has been declared in a United States District Court proceeding between Heublein and Allied to be null, void and unenforceable and is no longer in effect. Allied no longer has the right to share in United's profits nor does it have the right to representation on United's board of directors. Allied's designees on the United Board of Directors have resigned (Memorandum in Support of Motion to Certify Dismissal of Allied Grape Growers to the Commission dated September 12, 1978, p. 7, Exhibit A; RX 1248Z–26 through Z–28. See *supra* p. 7).

271. Allied has sold its 18 percent interest in Vintners to Heublein, and Vintners has been merged into Heublein leaving Heublein as sole owner of United (See *supra,* pp. 7, 9). [54]

272. Pursuant to an agreement (among Heublein, United, Allied and Vintners), Allied in late 1978 entered into a six-year grape supply contract with United (RX 1248A through Z–4).

V. THE RELEVANT MARKET

Determination of the relevant market is prerequisite to determination of whether a challenged acquisition does, in fact, violate the antitrust laws. An acquisition in violation of the law " . . . must be one which will substantially lessen competition 'within the area of effective competition.' Substantiality can be determined only in terms of the market affected." *United States* v. *duPont & Co.,* 353 U.S. 586, 593 (footnote omitted).

A. Geographic Market

273. The relevant geographic market in which the effects of

Heublein's acquisition of United Vintners are to be measured is the United States as a whole (Amended Complaint, Para. 19; Answers of Heublein and United Vintners to Paragraph 19 of the Amended Complaint).

B. Product Market

Brown Shoe Co. v. *U.S.,* 370 U.S. 294 (1962), set out the standards by which relevant product markets and submarkets are determined:

> The outer boundaries of a product market are determined by the reasonable interchangeability of use or the cross-elasticity of demand between the product itself and substitutes for it. However, within this broad market, well-defined submarkets may exist which, in themselves, constitute product markets for antitrust purposes. *United States* v. *E. I. duPont de Nemours & Co.,* 353 U.S. 586, 593–595. The boundaries of such a submarket may be determined by examining such practical indicia as industry or public recognition of the submarket as a separate economic entity, the product's peculiar characteristics and uses, unique production facilities, distinct customers, distinct prices, sensitivity to price changes, and specialized vendors. Because ¶ 7 of the Clayton Act prohibits any merger which may substantially lessen competition "in *any* line of commerce" (emphasis supplied), it is necessary to examine the effects of a merger in each such economically significant submarket to determine if there is a reasonable probability that the merger will substantially lessen competition. If such a probability is found [55]to exist, the merger is proscribed, . . . (at 325, footnotes omitted).

With *Brown Shoe* in mind, the following findings require the conclusion that the relevant product market is "all wines" and that "table", "dessert" and "sparkling" wines are "well-defined submarkets. . .which, in themselves, constitute product markets for antitrust purposes."

1. Product Market—Wine

274. "Wine", as defined for purposes of government regulation of wine production, winery construction, winery licensing, wine ingredients, wine taxation and related purposes, is an alcoholic beverage which is the product of the juice or must of grapes or other fruit. It includes products which have been sweetened or to which various flavoring ingredients have been added. Included are all still wines, champagne and other sparkling wines, artificially carbonated wines and special natural wines. Special natural wines are flavored wines such as vermouth made pursuant to a formula approved under government regulations (CX 309J, K, L; 26 U.S.C. 5381–5386).

275. There are literally hundreds of different kinds of wines (CX 308K). However, all wines are produced basically in the same manner, by crushing grapes or other fruit and fermenting their juice. The ensuing procedures then differ somewhat depending upon

the particular kinds of wines desired. For a description of production procedures, see Findings 406–12, *infra.*

276. Industry statistics such as those of the Wine Institute (the leading trade association in the industry) are maintained in three categories—(1) still wines containing up to 14 percent alcohol; (2) still wines containing over 14 percent alcohol; and (3) effervescent wines (Tr. 1579–80). The terms "dry", "table" or "dinner" wines are used for still wines not over 14 percent alcohol (Tr. 1812, 3153; CX 308Z–24, 310 O, P, Q). The terms "sweet", "dessert" or "appetizer" wines are used for still wines over 14 percent alcohol (Tr. 1812, 3153; CX 308L, 310 O, P, Q).[15] The term "dessert wines" also includes "appetizer wines" (CX 308L). Effervescent wines include artificially carbonated wines (CX 309J). The term "sparkling" is used to refer to effervescent wines (Tr. 1812; CX 308R). Examples of table wines are Burgundy, Gamay, Cabernet Sauvignon, Ruby Cabernet, Pinot Noir, Zinfandel, Pinot Chardonnay, Chenin Blanc, Emerald Riesling, Grey Riesling, Chianti, Sauterne. Examples of dessert wines (including appetizer wines) are Sherry, Vermouth, Port, Tokay and Muscatel. Examples of sparkling wines are Champagne and Sparkling Burgundy (CX 308K). [56]

277. Wines are also classified as generic or varietal. Varietal wines are named after the predominant grape variety contained in the wine and by law must contain at least 51 percent of that grape variety (CX 310S; Tr. 749). Examples of varietal wines are Cabernet, Pinot Noir, Zinfandel, Chardonnay, Riesling, Muscatel, Ruby Cabernet, Petit Sirah, French Columbard, Emerald Riesling, Barbera, Sylvaner and Chenin Blanc (CX 308Z–24; Tr. 540A). Generic wines may be made from a mixture of grapes, no one of which need account for any specified percentage of the grapes used (Tr. 757). Examples of generic wines are Burgundy, Rhine Wine, Sherry, Port, Sauterne and Chablis (CX 308Z–23; Tr. 757).

278. Varietal wines contain from 51 percent to 100 percent of the varietal grape for which they are named. There is no requirement that the varietal percentage be disclosed on the label (Tr. 517) and such disclosure is not usually made (Tr. 811). There is no indication with respect to generic wines of the types of grapes used in their production (Tr. 810).

279. All wines vary in quality depending on where, when and how they are made. There are wide ranges of wine quality. There is variation within types of wines and within wineries. There is a continuum of wine quality. A particular wine can vary among

[15] The terms "sweet" and "dry" refer to alcoholic content, not to the taste of the wine (Tr. 1812; CX 308Z–24).

various producers, and for a single producer from year to year. There are thousands of variations in the winemaking process. Time, temperature, and winemaking procedures all affect the gradation in wine quality. The very same variety of grapes differs in quality and this causes variations in the wine produced from them. The wine handling ability of a winery also affects wine quality (Tr. 523, 532–33, 758, 913, 3153).

280. The range of prices for all kinds of wines also varies (Tr. 2873). Cabernet Sauvignon wines, for example, range in price from under $2.00 a bottle for Italian Swiss Colony up to $20 per bottle (Tr. 758). The price range of generic wines overlaps the price range for varietal wines (Tr. 2874–75). The wines of United in January 1974 ranged from $.99 to $6.50 per 1/5 gallon bottle at California retail prices (CX 218Z–291 through Z–304). In 1972, United's product line sold over a retail price range of $.89 or $.95 to $5 or $6 a bottle. There were very few price gaps and United sold products at virtually every pricing point (Tr. 3741).[16] In California, Gallo prices are near the lowest end of the price range and Beaulieu prices are near the upper end (Tr. 1849). About 2 percent of wines sell above Beaulieu's prices and about 10 percent of wines sell [57]below Gallo's prices (Tr. 1853). As of January 1974, the California retail price range of Gallo wines was from $.69 to $2.79 per fifth (CX 218Z–280, 218Z–281), while that of Beaulieu wines was from $2.25 to $7.00 (CX 218Z–263).

Price—Quality Considerations

281. Wines were referred to by numerous witnesses as "standard" or "premium". Some of those witnesses did so on the basis of wine quality (Tr. 673, 674, 774, 1871, 2214, 2215, 2154). Others applied the terms "standard" or "premium" according to price (Tr. 1712, 2035, 3473, 3930, 4249, 7252, 9760–61, 9983, 9984).

HUV contend that the effects of the challenged merger must be analyzed on the basis of separate "standard" and "premium" wine submarkets. Their proposed categorization is based on alleged price differences (Tr. 10329–33; RX 1D, 1E, 7C, 7D, 9D, 15B, 17G, 23E, 25E, 27B).

282. With reference to December 1972 California wine, for example, HUV have classified table wines retailing at under $1.35 per fifth as standard and those selling at $1.35 and above as premium (RX 1D, 1E, 17G), "sweet" wines selling at $1.35 per fifth as standard and those selling at $1.35 and above as premium (RX 7C, 23E),

[16] Another example of price range is Guild Wineries and Distillers whose table wines sell at retail from $1.09 to $4.50 (Tr. 2991).

sparkling wines selling at under $3.49 per fifth as standard and those selling at above $3.49 as premium (RX 9D, 25E), and refreshment wines selling at under $1.35 per fifth as standard and those selling at $1.35 and above as premium (RX 15B, 27B).

283. Witnesses who characterized wines as standard or premium on the basis of price differed in their price divisions. Marvin Sands, President of Canandaigua Wine Company, views Gallo's $1.69 price as the upper end of the standard price range and the $1.79 to $2.50 prices of Almaden, Paul Masson and Christian Brothers as the beginning of the premium price range (Tr. 4249). Louis Gomberg, wine consultant who prepared various tables for HUV, used $1.25 in his industry statistics as the dividing line for table and dessert wines and $3.50 for sparkling wines in 1970. These dividing lines were increased over the years to account for inflation and were $1.45 and $4.00 respectively, in 1971, $1.50 and $4.00, respectively, in 1972, and $1.75 and $4.50, respectively, in 1973. In 1974, Mr. Gomberg's table and dessert wine dividing line was $2. In 1975 and 1976, his dividing lines were $2 for table and dessert wines and $4.50 for sparkling wines (Tr. 1817–22; RX 581, 585, 586). Ralph Hart, former president, chief executive officer and chairman of the board of Heublein defined premium wines as those selling for $3 to $6 as of the time he was chief executive officer of Heublein (Tr. 3930). Mr. Hart was chief executive officer of Heublein until April 1968 (Tr. 3921). [58]

284. Dr. Richard Peterson, winemaster and president of the Monterey Vineyard, is also president of the American Society of Enologists, the scientific and professional society for winemakers (Tr. 320, 325). In Dr. Peterson's opinion, the term "premium" means different things to different people. Henry Rubin, a wine columnist and wine consultant, would not define "premium" because it is a very loosely used term. Any winery can call its wines "premium", and many do as a matter of self-evaluation. This, however, does not mean that they are of any higher quality (Tr. 721, 773–74).

285. Wine price may not be relied upon as an indicator of quality (Tr. 514). Most marketers agree that retail price depends far more on volume than on actual product quality (Tr. 514, RX 1184B). Certain wines such as the second line of Almaden and Sebastiani are marketed in a manner intended to make the consumer believe they are "premium" wines or "sublevel of premium" wines, but are actually "standard" wines (Peterson Tr. 1871). Almaden mountain wines and the Inglenook Navalle wines are both "standard" wines dressed up as "premiums" (Peterson Tr. 1877).

286. There is only a loose relationship between wine quality and price (Tr. 753). There is no absolute line between low-priced and

high-priced wines (Tr. 773). Henry Rubin as a writer on wines assesses the quality of wines against their prices and advises consumers which wines are a good value (Tr. 772). He testified that some wines, such as Lancers and Blue Nun, are overpriced for their quality (Tr. 753), while others are underpriced for their quality (Tr. 754).

287. Robert Balzer, a former wine store owner and restauranter, is a wine writer with a nationally syndicated column in the Los Angeles Times and is the food and wine editor for Holiday magazine (Tr. 2791–95). He circulates a newsletter on food and wine and has written a number of books on wine (Tr. 2795–96). He has taught five courses on wine at UCLA (Tr. 2799). He is acquainted with consumer tastes and purchasing habits in wine through his 27 years as a wine merchant, teacher, his restaurant experience and hundreds of letters each month from his wine consumer readers (Tr. 2791, 2799–2800). He is an experienced wine taster who participates in 75 to 100 wine tastings a year and who conducts monthly wine tastings by panels of competent and experienced tasters for his newsletter (Tr. 2803–08). He was presented to the public by United as a wine expert in an advertisement for Inglenook (RX 331B). The tastings for his newsletter include low-priced and high-priced wines (Tr. 2821). The quality evaluation of wine at the tastings is based upon a generally accepted and recognized 20 point scoring system developed at the Department of Viticulture and Enology at the University of California at Davis (Tr. 2808, 2840, [59]2919–22). The wines so evaluated are ranked on the basis of their quality in his newsletter (Tr. 2821–22; CX 346, 347, 348, 349, 350).

288. The prices of wines which are rated in Balzer's tastings do not follow quality rankings, but vary. The retail price of wine is not a reliable index of wine quality (Tr. 2842, 2860; CX 346, 347, 348, 349, 350). The broad range of wines which are evaluated in Balzer's newsletter irrespective of price are wines from which a consumer would choose and are thus in competition with one another (Tr. 2868, 2869).

289. As an example of the variance in the price-quality relationship, ten brands of the same variety of wine, Cabernet Sauvignon, each selling for $3 would not have the same quality (Tr. 7256, 7258, 7259).

290. In comparative blind tastings by experts and novices of California and European wines, California wines were preferred although the imports frequently cost two to three times as much as their California counterparts (CX 308Z–1 thru Z–8).

291. Imported wines and California wines are similar in charac-

teristics and are made from the same types of grapes grown under similar conditions (CX 308U). California wines are made from the European grape family called *vitis vinifera* (CX 308T, 308Z–14 thru Z–16). John Powers, chairman of the board of United Vintners, confirmed that imported and domestic wines compete with each other within industry segments (Tr. 9825). Wines produced in the eastern and midwestern states are made from grapes of the family *vitis labrusca,* the native American grape. Both HUV and complaint counsel have included wines from all geographic areas within the relevant markets as they have defined them (RX 1D; CX 373A).

292. Heublein's own 1967/68 Marketing Plan (CX 97K, L, M) demonstrates the invalidity of HUV's present contention that "standard" and "premium" wines must be treated as separate markets. There, it was recognized that competition for Heublein's Harveys Bristol Cream (a "premium" wine) came from three sources:

1. The premium quality imported sherry market.
2. The imported liqueur-cordial market.
3. The domestic "fifth" sherry trade-up market. [60]

After reciting that Harveys' prime competition comes from other imported sherries, and that, because of its high quality, premium price and position acquired by advertising effort, it was also in competition with quality cordials and liqueurs, it was concluded:

Also, because of the sizeable volume and potential of the domestic "fifth" sherry market, brands such as Gallo's, Taylor, and Paul Masson cannot be overlooked as competition to Harvey's Bristol Cream. This could be a trade-up market for Harvey's. It is noteworthy that connoisseurs have judged the quality of these domestic sherries to be as good as or equal to the quality of some imported sherries. (See opposite for comparison of prices in these three categories.)

The prices referred to (Retail in California) were $.82 for Gallo (well below HUV's "standard"—"premium" price demarcation); and $1.75 for Taylor and $2.87 for Paul Masson. Also listed was Almaden at $1.48. Yet Heublein considered all such wines to be in competition with its Harveys brand which sold for $6.89.

Physical Characteristics

293. Wine has unique physical characteristics. The federal government has established standards of identity for wine (CX 308Z–7, 310N–Q). Wine is a beverage containing by law from 7 percent to 24 percent alcohol (CX 310J).

294. The sensory evaluation of wine is called organoleptic

evaluation (Tr. 462). Organoleptic evaluation is used to assess the physical characteristics of wine such as clarity, aroma, bouquet, color, flavor, acidity, presence of acetic acid, sweetness and other factors (Tr. 2911–18, 738). There is a generally accepted standard used worldwide for evaluation of the physical characteristics of wine called the Davis 20-point scale (Tr. 2840, 2921).

295. Wine is the only beverage which offers the complete range of the four tastes to which the palate is sensitive—sweetness, acidity, saltiness and bitterness (CX 308D).

Wine Production

296. Wine of all types—table, dessert, and sparkling—are generally produced by the same group of firms. Each of the eight largest firms for wine overall in 1972 (CX 373K) produced table, sparkling and dessert wines. **[61]**

1. Gallo (CX 373U, Z–7, Z–13).
2. Heublein (United Vintners) (CX 373U, Z–7, Z–13).
3. National Distillers (Almaden) (RX 23A; CX 373Z–7, Z–13).
4. Guild (CX 373U, Z–7; RX 10A).
5. Mogen David (CX 373U, Z–7; RX 26C).
6. Taylor (CX 373U, Z–13; RX 18A).
7. Franzia (CX 373Z–7, Z–13; RX 7A).
8. Seagram (Paul Masson) (CX 373Z–7; RX 23A, 25A).

297. Every firm which is among the eight largest firms in the table, dessert or sparkling wine category (but not in the all wine category) is a producer (or importer in the case of Renfield Importers) of all three categories of wine: table, dessert and sparkling.

Canandaigua Industries	(CX 373U; Tr. 4192–93)
Renfield Importers (imports)	(CX 373U; RX 17D, 26A)

The Christian Brothers	(CX 218Z-270, 373U)
Monarch Wine Co.	(CX 373Z-7, 373Z-13; RX 1B)
Gold Seal Vineyards, Inc.	(CX 373Z-13; RX 17A, 233)

298. Vermouth, a still wine over 14 percent in alcohol, was produced by seven of the eight leading firms in the all wine category for 1972 (CX 373K).

1. Gallo	(CX 218Z-280)
2. Heublein (United Vintners)	(CX 218Z-292, Z-285)
3. National Distillers (Almaden)	(CX 218Z-292, Z-262)
4. Guild	(CX 218Z-287)
6. Taylor	(CX 168D (1968))
7. Franzia	(CX 218Z-278)
8. Seagram (Paul Masson)	(CX 218Z thru 266)

299. The fifth ranked firm, Mogen David, is owned by the Coca Cola Bottling Company of New York which also owns Vermouth Industries of America.

300. With certain modifications in physical plant, wineries can shift their production from one type of wine to another in response to changes in demand. This was done by United, which made changes in its wineries in the 1960's to meet the change in demand from dessert wines to table wines (Tr. 2585, 2619, 2620, 2637). The Escalon winery was converted from a dessert wine plant to a table wine plant (Tr. 2619). Gallo converted its wineries to emphasize the production of table wines (Tr. 440). The Monterey Vineyard [62]winery was not designed with sparkling wine capability but could have added equipment to produce champagne. It could also have produced dessert wine simply by adding some tanks (Tr. 531). The industry as a whole shifted its production in the 1960's from dessert to table wine (Tr. 439, 7466-67, 8090).

301. Many firms including the industry leaders, Gallo and United, produce both, what have been termed, "standard" and "premium" wines. The following firms have been described as producing both such wines: Geyser Peak (Tr. 6274); California Wine Association (Tr. 1014); United Vintners (Tr. 3741, 9530-31); Guild (Tr. 3047-48); Weibel (Tr. 673, 716); Gallo (Tr. 9807, 9971); California Growers (Tr. 1954); Canandaigua (Tr. 4198); Angelo Papagni (Tr. 6276-77); Montcalm (Tr. 5162, 5244); Heublein (Tr. 2856); C. Mondavi (Tr. 1720); Almaden (Tr. 1870, 1871, 1877); and Sebastiani (Tr. 1870, 1871).

302. There is a trend toward expansion of the price and quality ranges sold by individual wineries (Tr. 767). Producers of low priced wines have extended their product lines upward in price and quality. In the last five years, Gallo has expanded the price range and quality range of its products (Tr. 1720, 1857–58, 1998–99, 3080–81, 8571–72).

303. New varietals have been added to the Colony brand of United. These include Cabernet Sauvignon, Pinot Noir, Chenin Blanc, Ruby Cabernet and French Columbard (Tr. 8568). They sold at higher prices than other Colony table wines (CX 536F).

304. Producers of high priced wines have extended their product line downward in price and quality. Almaden in the 1960's bottled its mountain wine in half gallon jugs. Other companies followed and the so-called "premium" category was downgraded in price (Tr. 1871–72). Witnesses referred to this middle price range as bridging the gap between "standard" and "premium" or between low priced wines and high priced wines (Tr. 1512, 1513, 1871–72, 8847–88, 8986; CX 192A). This medium price range was sometimes referred to as "subpremium" (Tr. 1513, 8986, 9477) or "midpremium" (Tr. 7259, 7596). Other terms sometimes used for these medium priced wines are "low end premium" or "mountain wine" (Tr. 1512–14). Companies in addition to Almaden producing wines in this price range together with higher priced wines are: Taylor (Tr. 8414); Paul Masson (Tr. 539, 8340); Beringer (Tr. 539, 8339–40); Sebastiani (Tr. 539); C. Mondavi (Charles Krug & C.K. Mondavi brands) (Tr. 1720, 7595–96).

305. United Vintners introduced a lower priced and lower quality wine called Inglenook Navalle to extend downward its Inglenook "premium" line of wines (Tr. 9272–73, 7834–35). [63]

306. Firms have shifted their production into this medium price range of wines in response to an increase in consumer demand (Tr. 8576). For example, the Inglenook brand of United had been exclusively in the high-priced range up to approximately 1971. By 1978, its production in table wine had shifted so that 3.4 to 3.5 million cases were the medium-priced Navalle and only 460,000 cases were in the higher priced Vintage and Estate lines. This constituted a shift in the line from 100 percent high-priced wines to 12 percent high-priced wines and 88 percent medium-priced wines (Tr. 8525, 9272–73).

307. The upper end of the Italian Swiss Colony ("standard") table wine price range in 1978 was $1.79. The low end of Almaden's ("premium") table wine price range was $1.89 (CX 536B, F). United's ("standard") Lejon champagne sold at $3.39 while Almaden's ("premium") Le Domaine champagne sold at $3.55 (CX 536B, F).

Production Expertise

308. Enology is the science of winemaking (CX 308Z–8). Viticulture is the science of grape growing (CX 308Z–8). There is a Department of Enology and Viticulture at the University of California at Davis (Tr. 3101).

309. Graduates of the department are employed in wineries both in the north coast area of California and the San Joaquin Valley area of California (Tr. 3101–02). (See Findings 312–27, *infra,* for discussion of significance of these two areas.)

310. Dr. Richard Peterson was responsible for winemaking at Gallo and left to become winemaster at Beaulieu (Tr. 329), Gallo was producing wines which Dr. Peterson characterized as "standard", while he considers Beaulieu to be the top chateau in California producing "premium" wines (Tr. 330, 502, 508). Gallo's wine handling ability is excellent and Gallo could produce high quality wines by using higher quality grapes (Tr. 532).

311. There is a professional society of winemakers called the American Society of Enologists, to which virtually all winemakers belong (Tr. 325).

Grapes and Vineyards

312. The north coast or coastal area and Central Valley or San Joaquin Valley area of California are grape growing and wine producing areas (Tr. 415, 425, 510, 1018–19, 1028, 1286, 3101–02, 3225–27, 4114, 7644–47). The Central Valley area includes the San Joaquin and Sacramento Valleys of California. The north coast includes Humboldt, Marin, Mendocino, Napa, Sonoma, Alameda, Contra Costa, Monterey, [64]San Benito, San Francisco, San Mateo, Santa Clara and Santa Cruz Counties (CX 296G). The geographic boundaries of the northcoast or coastal area have been expanding over recent years (Tr. 1286).

313. In the mid 1940's to mid 1960's the so-called "premium" wineries such as Paul Masson, Christian Brothers and Inglenook used grapes from the coastal area rather than the Central Valley (Tr. 7476). Today, however, firms rely substantially on grapes grown in the Central Valley to produce "midpremium" wines (Tr. 7612).

314. The northcoast wineries are substantial users of Central Valley grapes. The following wineries identified by witnesses as northcoast or "premium" wineries use Central Valley grapes or wine made from Central Valley grapes. Robert Mondavi; Charles Krug (C. Mondavi); Paul Masson; Christian Brothers; Almaden; Sebastiani;

Inglenook (United Vintners); Hans Kornell; and Weibel (Tr. 510, 717, 4114, 7644–46, 7834–35, 7951–52).

315. Almaden, the leading producer of mountain table wine (RX 18A) had 75 percent of its table wine sales in its Mountain Wine line (CX 289C). The grapes for this line came almost exclusively from the San Joaquin Valley (Tr. 956). The Almaden winery is in the north coast area, but the sources of close to 75 percent of its table wines are wineries such as Pirelli-Minetti, Gallo, Sierra Wine Company and Delicato, all located in the San Joaquin Valley (Tr. 928–32; CX 464E). The varietal grapes owned by Almaden comprise only 10 percent of its grape requirements. Sierra Wine Company located in the Southern San Joaquin Valley accounts for 40–50 percent of Almaden's grape or wine requirements (CX 464E). Inglenook competes for the same grapes as Gallo (Tr. 950).

316. Inglenook's Navalle line of wines which comprises about 88 percent of the Inglenook table wines is made in substantial part from Central Valley grapes (Tr. 7951–52). Among United's "premium wine" production facilities is the winery at Escalon in the Central Valley (Tr. 8509–10). Escalon is used primarily for the production of Inglenook Navalle wines (Tr. 9946). The Lodi facility which is a part of the so-called Premium Wine Company of United is also located in the Central Valley (Tr. 8509–10).

317. Some Central Valley wineries do nothing but produce wine for north coast wineries (Tr. 1028). Central Valley wineries which shipped wine to coastal wineries include: Sierra Wine Company; Delicato Winery; California Wine Association; California Growers; Cherokee Vineyard Association; and Gallo (Tr. 928, 932, 1015, 1028, 1959, 7645–46). [65]

318. The movement of Central Valley wine and grapes to north coast wineries increased in the late 1960's (Tr. 4109, 4112).

319. In 1968, the southern and central San Joaquin Valley accounted for 52.6 percent of all wine produced in California. In the same year, the Escalon-Modesto area accounted for 21.2 percent and the Lodi-Sacramento area 9.3 percent. The north coast areas of California were responsible for 14.5 percent, while Southern California represented 2.3 percent of total wine production for the state (CX 291H).

320. In 1971, the southern and central San Joaquin Valley accounted for 57.4 percent of all wine produced in California. In the same year, the Escalon-Modesto area accounted for 20.1 percent and the Lodi-Sacramento area 8.0 percent. The north coast areas of California were responsible for 12.6 percent, while Southern California represented 1.9 percent of the state's wine production (CX 296I).

321. From 1968 through 1971, the Central Valley area of California, including the southern and central portions of the San Joaquin Valley as well as the Escalon-Modesto and Lodi-Sacramento districts, accounted for 82.6 percent to 87.3 percent of total California production of all wines. During the same period, the north coast areas produced 11.4 percent to 14.5 percent of total California production of all wines (CX 291H and 296I).

322. It is now common practice for wineries outside the Central Valley to purchase grapes from there (Tr. 931). Without Central Valley grapes such firms could not produce as much wine as they do (Tr. 932). Dr. Richard Peterson estimated that 90 percent of the wine grapes crushed in California came from the San Joaquin Valley (Tr. 510).

323. Central Valley wineries use grapes or wine from the north coast (Tr. 1018–19, 2216, 3225, 4114, 7646–47). Gallo is one of the largest purchasers of grapes and wine in the Napa Valley, one of the areas in which the finest grapes are grown (Tr. 415, 520). Gallo also purchased wines from Sonoma and Mendocino Counties (Tr. 4115). Gallo owns the Frei Brothers winery on the north coast and purchases wines from the Napa Coop in that area (Tr. 7647).

324. Both Gallo and United are large purchasers of grapes on the north coast to the point of affecting the prices others must pay for north coast grapes (Tr. 2216, 2219, 2253–54; CX 438). **[66]**

325. The Monterey Vineyard grape acreage is planted to so-called "premium" or varietal grapes. Gallo purchases about one-third of this supply, while the remainder is purchased by Robert Mondavi, Wente, Mirassou, Sebastiani and others (Tr. 519–20). Dr. Peterson identified Robert Mondavi, Wente and Mirassou as producers of "premium" wine and Sebastiani as a producer of "premium" and "subpremium" wines (Tr. 502, 539).

326. Napa Valley and Central Valley grapes are blended in various percentages and result in wines, including generics, of various quality levels (Tr. 526). The blending of wines is a complicated command decision of the winemaker who may blend wines from different varieties of grapes, from different districts and from different years. Every winemaker blends wines differently (Tr. 3150). Blending in the making of varietal wines varies considerably from winery to winery (Tr. 3150–52).

327. Dessert wines of all qualities are produced primarily from Central Valley grapes (Tr. 525).

Industry Recognition

328. The Wine Institute is a voluntary trade association comprised of wineries from all areas of California.[17] Its members produce wines of all types and at all prices (Tr. 564–65, 2992). Members are not classified according to the prices at which their wines are sold (Tr. 2992). About 90 percent of winery license holders are members of the Wine Institute (Tr. 974). Its purpose is to increase public awareness of wine and to expand the market for it (Tr. 567–68). It is the leading wine industry trade association in the United States (Tr. 582).

329. One of the Wine Institute's functions is to compile statistical data to enable the industry and others to understand the industry's posture, *i.e.*, what is going to market, what is likely to go to market and industry trends in terms of kinds of wines (Tr. 585–86). The statistical surveys were started by Louis Gomberg while he was with the Wine Institute and were intended to inform industry members, grape growers, suppliers to the industry, government agencies and universities of activities occurring in the industry (Tr. 1578–79). [67]

330. Members of the wine industry refer to the Wine Institute statistics for industry statistical information. The statistics are considered reliable and are relied upon by members of the wine industry (Tr. 590, 591, 977).

331. As originally prepared in the 1930's and 1940's, the statistical reports were broken down into three basic categories: up to 14 percent alcohol, over 14 percent alcohol, and effervescent. These categories are essentially the same today (Tr. 1578–80). Wine industry statistics are still broken down according to tax categories. Wines under 14 percent are table wines and include the so-called refreshment wines. Wines between 14 percent and 21 percent are aperitif and dessert wines. The third category is sparkling (Tr. 592). The category "all wine", the total of table, dessert and sparkling wines, is reported in the statistical reports and includes both domestic and imported wine (Tr. 979; CX 295 (Table 6)). The Wine Institute statistical reports have never been broken down by price categories nor by "standard" and "premium" classifications (Tr. 980–81; CX 291–92).

332. The Wine Institute has an economic research department to forecast market trends and probable raw material needs for the

[17] California is the largest wine producing area in the United States, followed by New York (CX 293H). California production as a percent of total United States commercially produced wine entering distribution channels in the United States was as follows: 84.6 percent in 1960, 81.5 percent in 1968, 84.9 percent in 1969, and 85.7 percent in 1976 (CX 295N, 366L; Wine Institute Bulletin, March 24, 1978, No. 78–3, Table 2, officially noticed September 27, 1978).

future. The economic research department develops the statistical data published by the Institute (Tr. 585, 972).

333. The Wine Institute has taken public positions on behalf of the California wine industry (Tr. 571). It has a trade barriers program and committee which is concerned with laws, regulations and proposed legislation in local, state and federal jurisdictions which would affect the entire wine industry (Tr. 3026–36).

334. The California Wine Advisory Board was a state board that administered a state marketing order for wine. It was in existence from 1938 to 1975 (Tr. 965). All producing wineries in California were assessed to provide funds for the Board (Tr. 969–70).

335. The programs of the Wine Advisory Board included promotion of California wine and generic advertising of wine, without the use of brand names. There were also programs dealing with trade barriers, economic research and statistics. The Wine Advisory Board for a time prepared the statistical reports that are now prepared by the Wine Institute (Tr. 966, 972).

336. There is a trade magazine for the wine industry called *Wines and Vines.* It reports on the California, United States and world wine industry (Tr. 2992). *Wines and Vines* publishes an annual directory of the United States wine industry listing winery capacities (Tr. 1745). [68]

337. Respondent Heublein has recognized "all wine" as a market. E.W. Kelley, Executive Vice President of Heublein commissioned McKinsey and Company to study United Vintners and the wine industry (Tr. 4533; CX 220). The study was prepared by McKinsey employees and by Andrew Beckstoffer who was on Kelley's staff and was Heublein's Manager of Acquisition Analysis (Tr. 4533, 8945). The McKinsey study was first reviewed by Kelley and then presented to the top management of Heublein (Tr. 4529–30, 4978). The study depicted the growth in the overall wine market (CX 220E). It compared the growth rates of individual companies such as Paul Masson, Almaden, Christian Brothers, Beaulieu, Gallo and Roma on the basis of all wine (CX 220H).

338. In discussing "Competitive Structure" and the relative size of competitors, the McKinsey study states: "Except For United Vintners And Gallo, Industry Is Composed Of Many Small Competitors," and lists as competitors United Vintners, Gallo, Taylor, Almaden, Paul Masson, Christian Brothers, Beaulieu, Beringer Brothers, Korbel, Wente, Martini and imports (CX 220I). This list includes both "standard" and "premium" producers, the distinct categories now contended for by HUV (RX 1, 17). The market shares of these firms and of imports as a whole are then presented as

percentages of the total dollar sales and case sales for all wines sold in the United States (CX 220I). In presenting a picture of wine production, the statistics used are for all wines and are not subdivided by type or price (CX 220K). United's market share in major geographic areas is presented as a share of the total United States wine market (CX 220Q).

339. In a proxy statement to its shareholders in connection with the acquisition of United, Heublein's and United's market shares are listed as percentages of total industry gallonage in the categories of still wines and champagnes. No distinction is drawn between price or quality classifications (CX 55Y).

340. In the section on "Competition and Regulation," the proxy statement states generally that "The wine industry is highly competitive and its productive capacity is substantially greater than the present rate of consumption." No distinction is made among product types or prices (CX 55Z).

341. There are no wine universe statistics prepared for industry use which are broken out between "standard" and "premium" (Tr. 10,044, 10,047, 10,337–38).

342. Heublein made a presentation to the Federal Trade Commission staff during the investigation which preceded this proceeding and voluntarily furnished additional documents supplementing the oral presentation (CX 327A, B). The documents discuss the competitive position of United Vintners [69]in terms of United's market share of the total domestic wine market, the domestic table wine market, the domestic sparkling wine market, and the market for all other domestic wines (CX 327U, Z–35). These same markets were used in discussing United's market share of wines sold in various states (CX 327V, W, Z–36 thru Z–40).

343. United also recognized the "all wine" market. Richard Oster, when he was president of United, justified a budget request by using charts reflecting United's share of market (Tr. 7809–10). The charts he used show United's and Gallo's share of the total United States wine market and is not subdivided into price or product categories (RX 1247B–C). In a talk presented to Heublein's management committee, Oster described United as "a strong number two factor in the United States wine industry" (Tr. 8000).

344. Mr. Oster's monthly reports to Stuart Watson, Chairman of the Board of Heublein, reflect that United's management monitored and reported United's performance in terms of its share in the all wine market (CX 238C, 239C, 240D, 241D, E, 242C, 243D, 244D, 246E).

345. Mr. Oster's successor, John Powers, is Chairman of the Board and Chief Executive Officer of United (Tr. 9420, 9425–26). Mr.

Powers continues to monitor United's performance in the "all wine" market. In another proceeding, Mr. Powers responded to a question as to United's market share, by giving United's share in the all wine market—at that time 18 percent. Upon further questioning he was unable to state United's market share in product or price categories such as "low", "standard" or "premium" (Tr. 9671–72).

346. Mr. Bruno C. Solari, President of United Vintners prior to the acquisition, was concerned about the entry of distilled spirits suppliers such as Seagram into the "wine business". He described Seagram as controlling 4 to 5 percent of the "wine business", without further categorization (Tr. 4686, 4688).

347. Robert Ivie, President of Guild Wineries and Distillers, was Chairman of the Wine Institute from 1974 to 1977 and a director for the nine previous years (Tr. 2964, 2967–68). He was part of a Wine Institute group which made a presentation to the Cost of Living Council for relief from price controls (Tr. 2987, 2990).

348. The Wine Institute made the presentation for the wine industry. The industry recognized that those of its members permitted under price control regulations to raise prices could not do so because "a significant pricing factor in the wine market," Gallo (whose prices were at the low end of the spectrum), was prevented by regulation from raising its prices. The industry recognized that, as a practical [70]matter, other firms could not raise prices as long as Gallo was precluded by regulation from raising its prices. Other members of the industry were thus deterred from raising their prices to reflect their costs, as permitted under the pricing regulations. This presentation of the industry position was made on behalf of all members of the Wine Institute including those whose wines were high priced, and was supported by the "premium" wineries (Tr. 2987–90). Other presentations requesting relief from price controls for the "wine industry" were made by the Wine Institute (see, *e.g.*, CX 313).

Government Recognition

349. The federal government has a 4-digit standard industrial classification number for all wine (CX 318).

350. The Federal Alcohol Administration Act and regulations thereunder make no distinctions among price categories of wine (Tr. 4104–05; CX 310). Neither do the Internal Revenue Code regulations applicable to wine (CX 309). The federal excise tax rates applicable to wine vary with product type, but not according to wine quality or price (CX 363A–B).

351. The California Board of Equalization uses tax categories of still wine not over 14 percent, still wine over 14 percent and sparkling wine, but makes no distinctions between "standard" and "premium" wines or price categories (Tr. 1727, 9696–97). The California marketing order for wine which was administered by the California Wine Advisory Board applied to all California wineries producing wine (Tr. 581, 582).

Common Channels of Distribution

352. In most instances, "standard" and "premium" wines pass through the same wholesale channels of distribution (Tr. 9738). Most wholesale distributors for Inglenook ("premium") wine were also Italian Swiss Colony ("standard") distributors (Tr. 7952–53). In 13 of the leading 15 metropolitan markets for wine, 24 out of 34 United distributors carried both Inglenook and Italian Swiss Colony wines (CX 533A). Over 70 percent of United's distributors carry both its "standard" and "premium" table wines (Tr. 9881). United's company-owned distributors in the Southern California and New York/New Jersey areas distribute both "standard" and "premium" wines (Tr. 9718–19, 9743).

353. Of the six distributor witnesses who categorized wines as "standard" or "premium", four carry both "standard" and "premium" wines (Tr. 3409, 6159, 6174, 6549, 6575, 7313–14; CX 400A, B). The sales forces of wholesale distributors are [71]responsible for sales of high and low priced wines and all product types (Tr. 3437, 6649–50, 7430; CX 400).

354. All wine companies compete with one another for wholesale distributors (Tr. 1084). Mr. Bruno C. Solari, former president of United, who testified that United's low priced wines and Seagram's high priced wines did not compete, feared Seagram's entry into the wine business (Tr. 4686, 4693–94, 4766–67). He felt that distribution of United's low priced wines would be foreclosed to certain distributors who carried the higher-priced Seagram's wines (Tr. 4686, 4689, 4693–94).

355. In at least eight control states, the state is the only distributor. Thus all wines must pass through the same distribution system all the way to the state retail stores (Tr. 9623–24; CX 379 O).

356. Wines of all types are sold through the same retail channels of distribution. Retail package stores carry both higher priced and lower priced wines (Tr. 3437, 6305, 6306, 7622, 8541, 9737). Grocery stores and supermarkets also carry both "standard" and "premium" wines (Tr. 3437, 8541, 9737).

357. The wine buyer for 130 stores of a California grocery chain testified that the range of wine prices in these stores was $.83 per fifth to $5 per fifth retail. He was allotted a limited shelf space for all wines in general (Tr. 2047, 2050–52, 2060).

358. All wines compete for shelf space and displays in retail stores (Tr. 655, 1084).

359. Both so-called "standard" and "premium" wines are carried by distributors for sales to restaurants (Tr. 1079–80, 6174–75, 6263, 6265–66, 6270, 6273; CX 400A, B).

360. Both fine wines and "jug" wines (sizes larger than one-fifth of a gallon) are sold in restaurants (Tr. 782). Fine wines on the wine list compete with the "jug" wine sold as a house wine. Customers vary their choices from time to time (Tr. 728, 782–83, 788–90, 2862). Inexpensive wines are sold to neighborhood restaurants and pizza parlors as house wines (Tr. 6262–65, 6310, 6574, 7321).

Consumer Understanding, Use and Buying Habits

361. Some consumers buy low-priced wines for all occasions, while others limit their purchases to high-priced wines. More customers, however, buy wines of varying quality and price (Tr. 776–77, 782, 2849–50, 7852). Consumers experiment by trying wines of various prices (Tr. 2974–75). Some join wine appreciation classes or groups (Tr. 728, 735–36, [72]2797–99). Even wine connoisseurs and other knowledgeable wine drinkers drink both high-priced and low-priced wines (Tr. 2851).

362. Consumers, considered collectively, think of wines over a wide range of price as suitable for a particular use, such as for drinking with a meal. This would encompass what might be considered low-priced, medium-priced and high-priced wines (Tr. 2977–78, 2984).

363. As testified by Dr. Barnes, HUV's economic expert witness, products subject to relatively frequent purchase "do tend to be regarded by consumers as sometimes substitutes for one another" (Tr. 10376).

364. Consumers may purchase a lower priced wine for everyday use and drink a higher priced or higher quality wine on special occasions, for example, when entertaining (Tr. 775, 2851, 2976–78, 2197). In restaurants, consumers may choose a lower priced house wine one time and a higher priced wine from the wine list the next (Tr. 783, 2862).

365. Consumers buy wine not on the basis of quality or price alone, but also on the basis of value in relation to price (Tr. 772,

2851). For example, a consumer who has tried both Gallo's Andre champagne at $1.98 and Korbel champagne at $6 might select either, or a different champagne. He would not necessarily choose the most expensive (Tr. 2316–17, 2330, 2332).

366. The determination of wine quality includes an element of subjective preference (Tr. 745, 2332, 2884). A consumer who prefers sweet-tasting wines might choose Gallo's lower-priced Andre champagne over the higher-priced and supposedly higher quality Korbel product because Andre tastes sweeter (Tr. 2332).

367. There is a learning curve for wine consumption. Consumers generally prefer sweeter wines when they first drink wine and move toward drier ones as they gain experience (Tr. 768–69, 2849, 5281).

368. Consumers commonly trade up in price and quality over time, purchasing the next higher grade or price category (Tr. 2975, 6281).

369. Trading up is a phenomenon that is recognized and exploited in the wine industry. Montcalm attempted to offer a full range of products for the consumer's maturing wine preferences (Tr. 5281). The maker of the more expensive Korbel champagne encourages trading up by consumers (Tr. 2335). "Standard" wine companies try to retain consumers who are trading up by offering varietal wines (Tr. 6281). [73]

370. United recognized the phenomenon of trading up. Richard Oster, United's former president, testified that Lejon champagne advertising was designed to trade up some consumers of lower priced wines (Tr. 7851–52). In Oster's judgment, Inglenook Navalle was directed at the person who wanted to trade up from "standard" wine to a "slightly better" product (Tr. 7949–50). Heublein's 1972 Annual Report stated that Inglenook wines were intended to capitalize on consumers' trading up as they gained knowledge of wines (CX 53 O).

371. Heublein realized that Harveys Bristol Cream competes not only with imported sherries, but also with domestic sherries, which a Heublein marketing plan called the "domestic 'fifth' sherry trade-up market" (CX 97K). In the section entitled "Competition", the marketing plan points out that Gallo, Taylor and Paul Masson cannot be overlooked as competition to Harveys Bristol Cream (CX 97L). At that time, the California retail price of Harveys Bristol Cream was $6.89, Taylor's was $1.75 and Gallo's was $.82 (CX 97M).

372. Consumers understand the term "premium" wine as constituting a quality claim (Tr. 774, 2854). "Premium" may be used by almost any winery under many different conditions and has no precise meaning to consumers (Tr. 839). "Premium" has been used in advertising and publications with reference to the wines of Gallo,

Italian Swiss Colony and Beaulieu, wines whose prices are vastly different (Tr. 839).

373. Gallo, whose products are low-priced, has long used the term "premium". In the late 1950's, Gallo undertook an extensive advertising campaign in which its wines were advertised as "premium" (Tr. 1647, 1648). Edward Shaw, a Young and Rubicam advertising agency executive responsible for Gallo's advertising, testified that Gallo used advertisements on nationwide television in 1973 and 1974 which described Gallo as a "premium" wine (Tr. 4887, 4889–90, 4892–95). The term "premium" was used in those commercials to convey a quality image of Gallo, its quality vineyards, grapes, and wines (Tr. 4895–96; Comm. Phys. Exh. Y, Z, Z–1, Z–2).

374. United itself has advertised its comparatively low-priced Italian Swiss Colony brands of wine as "premium". In an advertising brochure entitled "Fine Wines from Italian Swiss Colony," the Private Stock and Napa Sonoma Mendocino table wines were described as "premium table wines" (CX 333C, D). The label on Napa Sonoma Mendocino bottles also used the word "premium" (Tr. 1886). These wines are classified by HUV for purposes of this case as "standard table wines" (CX 1E).

375. United advertises its Italian Swiss Colony wines as coming from "premium wine country" (CX 333B). [74]

376. The original Italian Swiss Colony settlement emphasized in United's advertising was at Asti in Sonoma County, a part of the north coast area (Tr. 4094; CX 333B, 443A, B). The Italian Swiss Colony visitor center and tasting room are at Asti (CX 443A). Italian Swiss Colony wines are labelled as "made and bottled" at "Italian Swiss Colony, California," or use a San Francisco address (Comm. Phys. Exh. A, B, C, F). "Italian Swiss Colony, California," however, is only a post office address for United's winery at Madera, California, which is in the Central Valley (Tr. 4093).

377. Consumers do not use the term "standard" wine (Tr. 774, 2855). Robert Furek, a marketing employee of United for eight years and a former vice president for marketing of United, does not recall the term "standard" ever being used in advertising or promoting Italian Swiss Colony wines (Tr. 8528–29). The term "standard" is not used on wine labels (Tr. 795).

378. Label styles on bottles of widely distributed "standard" and "premium" wines are so similar that a consumer cannot determine which wine is "standard" and which is "premium" from labels (Tr. 795–96, 805–06, Comm. Phys. Exh. G, L). This was demonstrated on the record with respect to five widely distributed champagnes. Champagnes selling in 1974 for $1.99 (Andre), $2.79 (Gallo), $2.99

(Lejon), $5.25 (Almaden) and $5.59 (Korbel) could not be distinguished as "standard" or "premium" on the basis of labeling or type of bottle closure (Tr. 806–08, 822; CX 218Z–262, Z–280, Z–281, Z–294, Z–295; Comm. Phys. Exh. J, D, O, Q).

379. Both high-priced and low-priced wines come in cork-sealed bottles (Tr. 819). Gallo wines selling for less than $2.00, as well as other low-priced wines, are cork-sealed (Tr. 819). Franzia sells cork-sealed wines which are "standard", as does Geyser Peak in its Summit line which is "standard" (Tr. 6279–80). Many low-priced, low-quality imports are sold with cork-sealed bottles (Tr. 820; Comm. Phys. Exh. V, W).

380. Jug wines are those which come in larger than fifth size bottles, *e.g.,* gallon or half-gallon bottles (Tr. 756). The same wines are also sold in fifths (Tr. 879–80, 2867).

381. As of 1974, the following brands of wines which HUV classified in their market share tables as "premium" or "mountain" were sold in both fifth and larger size bottles:

Almaden	(CX 218Z–262, 440Z–259)
Paul Masson	(CX 218Z–266, 440Z–263)
Christian Brothers	(CX 218Z–270, 440Z–268)
Guild (Cresta Blanca)	(CX 218Z–272, 440Z–269)
Beringer (as of 1972)	(CX 218Z–277, 440Z–261) [75]
Harveys Bristol Cream	(CX 218Z–289, 440Z–226)
Lancers	(CX 218Z–290, 440Z–226)
United Vintners (Inglenook Vintage)	(CX 218Z–291, 440Z–279)
United Vintners (Inglenook Navalle)	(CX 218Z–291, 440Z–279)
Korbel	(CX 218Z–294, 440Z–278)
Mogen David	(CX 218Z–299, 440Z–285)
Monarch (Manischewitz)	(CX 218Z–300, 440Z–386)
Robert Mondavi	(CX 218Z–300, 440Z–286)
C. Mondavi (CK)	(CX 218Z–301, 440Z–287)
Sebastiani	(CX 218Z–309, 440Z–292)
Taylor (as of 1978)	(CX 485C, 440Z–127)
Wente	(CX 218Z–313, 440Z–293)
Louis Martini	(CX 218Z–212, 440Z–211)
California Wine Assoc. (Eleven Cellars)	(CX 218Z–265, 440Z–266)

382. As of January 1974, the following brands of wine which

HUV classified in their market share tables as "standard" were sold in both fifth and larger size bottles:

Franzia	(CX 218Z–278, 440Z–270)
Gibson	(CX 218Z–274, 440Z–275)
Gallo	(CX 218Z–280, 440Z–271)
Guild (Cribari and Winemasters)	(CX 218Z–287, 440Z–277)
United Vintners (Italian Swiss Colony)	(CX 218Z–292, 440Z–281)
United Vintners (Petri)	(CX 218Z–304, 440Z–289)
Guild (Roma)	(CX 218Z–305, 440Z–290)
California Growers (Growers)	(CX 218Z–286, 440Z–276)
California Wine Assoc. (L&J)	(CX 218Z–265, 440Z–266)

383. Consumers cannot distinguish between "standard" and "premium" wines on the basis of packaging because of the similarities in labelling, closure and bottle size (Tr. 824).

384. Only a limited number of consumers understand the difference between generic and varietal wines (Tr. 808–09). Neither generic nor varietal wine labels usually disclose the percentage of varietal grapes used in the wine (Tr. 810–11).

385. Vintage dating of wines may be misleading to the consumer attempting to determine the quality of wine (Tr. 813).

386. Wineries use d/b/a (trade) names on their labels. When d/b/a names are used, consumers cannot determine what company has actually produced the wine (Tr. 813). [76]

387. Under current regulations of the Bureau of Alcohol, Tobacco and Firearms, consumers are unable to determine where a wine was produced from the label on the bottle (Tr. 4100). Wine may be shipped from the Central Valley to the north coast area and be labeled as "produced and bottled" at a north coast location if a company owns facilities in both areas. In such a situation, 100 percent Central Valley wine may be designated as "produced and bottled" at the north coast location (Tr. 4143). Wine can be shipped from the Central Valley to the north coast and be labeled as "made and bottled" at a north coast location even if the firm selling the bottled wine has not made any of it (Tr. 4144, 4147).

388. The term "estate bottled" originally meant that a wine so labelled was produced entirely from grapes grown by the producer in vineyards within five miles of the winery. The term is now so loosely

used it has practically no meaning to the consumer (Tr. 811–12, 4051, 4058–60, 4073).

389. There is a spectrum of wine prices from which consumers may choose (Finding 280 *supra*). Wine prices do not fall in distinct groups with large gaps between them but constitute a continuous spectrum (CX 218, 440).

390. Burgundy prices are an example of the continuum. Burgundy is a common generic red table wine named after the Burgundy region of France. Domestic wines with similar characteristics are called burgundies (CX 308K, L). Burgundies are available over a wide and continuous spectrum of prices (CX 218). A consumer selecting a burgundy is faced with a vast array of choices among brands and retail prices (CX 218):

$ .89	Gallo (Carlo Rossi)	(CX 218Z–281)
.99	United (Petri)	(CX 218Z–304)
	Franzia	(CX 218Z–278)
1.09	Guild (Cribari, Tavola)	(CX 218Z–289)
1.29	United (Italian Swiss Colony)	(CX 218Z–292)
1.29	Gallo (Gallo Burgundy)	(CX 218Z–280)
1.39	Gallo (Gallo Hearty Burgundy)	(CX 218Z–280)
1.59	Almaden (Mountain Red Burgundy)	(CX 218Z–262)
	United (Italian Swiss Colony Private Stock)	(CX 218Z–292)
1.69	United (Napa Sonoma Mendocino)	(CX 218Z–292)
	United (Inglenook Navalle)	(CX 218Z–291)
1.89	Almaden (Mountain Burgundy)	(CX 218Z–262)
1.99	Beringer (Beringer)	(CX 218Z–277)
	Paul Masson	(CX 218Z–266)
	Christian Brothers	(CX 218Z–270)
2.15	Sebastiani	(CX 218Z–309)
2.19	United (Inglenook Vintage)	(CX 218Z–291)
2.25	Korbel	(CX 218Z–294)
	Charles Krug	(CX 218Z–269)
2.50	Beaulieu Vineyard	(CX 218Z–263) [77]
2.75	Mirassou	(CX 218Z–299)
2.75	Heublein (Bouchard imported red	(CX 218Z–288)
29.15	Burgundies, 28 different selections)	

(Prices are per fifth bottle at retail in 1974 in California)

391. For 1974, HUV's proposed price cut-off between "standard"

and "premium" table wines is $2.00 (RX 585). HUV's position that a table wine selling for just under $2.00 would not be in competition with one selling for just over that amount (while at the same time acknowledging that all table wines selling at all prices under $2.00 would be in competition with each other and all table wines selling at all prices over $2.00 would be in competition with each other) is untenable.

392. Not only does the price of burgundy vary from brand to brand but also within any given brand. Burgundy is only one specific type of table wine among many others selling at different prices so that the prices of competing table wines have even smaller gaps than are demonstrated for burgundies alone (CX 218Z–262 thru Z–303, 308K, 440Z–258 thru Z–294). Each of the other types also varies in price between brands and from brand to brand (CX 218Z–262 thru Z–303, 440Z–258 thru Z–294).

393. United's own table wine prices illustrate the variety of prices at which table wines are available (CX 536E, F, I):

Petri

$1.19 Burgundy, Chianti, Chablis Blanc, Pink Chablis, Vin Rose, Rhine, Sauterne

Colony

$1.39 Alfresco Rose, Alfresco Blanc
$1.49 Rose, Rhineskeller, Moselle, Chianti
$1.59 Sauterne Blanc, Rhine, Burgundy, Emerald Chablis, Pink Chablis, Gold Chablis, Ruby Chablis
$1.69 Ruby Cabernet, Zinfandel, Barbera, Rhine Riesling, Chenin Blanc, French Columbard, Pinot Noir
$1.79 Cabernet Sauvignon
$2.49 Tipo Chianti [78]

Inglenook Navalle

$2.09 Burgundy, Chablis, Vin Rose, Rhine, Riesling
$2.19 French Columbard, Chenin Blanc, Zinfandel, Ruby Cabernet

Inglenook Vintage

$2.70 Burgundy, Chablis, Rhine, Cabernet Rose

Inglenook Estate

$3.75 Gamay Rose, Gamay Beaujolais, Zinfandel, Petite Sirah, Sauvignon Blanc
$4.00 Chenin Blanc, Grey Riesling
$5.00 Pinot Noir
$5.50 Gewuztraminer, Johannisberg Riesling, Charbono
$6.50 Cabernet Sauvignon, Pinot Chardonnay
$7.50 Red Pinot/Pinot St. George, Pinot Noir (Cask)
$8.50 Cabernet Sauvignon (Cask)

All prices are for fifth gallon bottles at retail in California in August 1978 (CX 536E, F, I).

394. Sherry is a common dessert wine (CX 308C). It is available over a wide and continuous spectrum of prices. A consumer purchasing a sherry faces many choices among brands and retail prices (CX 218). This range of choice was recognized by Heublein in its marketing plan for Harveys Bristol Cream where Gallo's $.82 sherry and Harveys at $6.89 are shown as competitors (CX 97K, L).

395. Champagne, a sparkling wine (CX 308C), is another example of a type of wine sold over a broad spectrum of prices (CX 218):

$ 1.95	Gallo (Andre)
	Franzia
	United Vintners (Jacques Bonet)
$ 2.49	United Vintners (Italian Swiss Colony Private Stock)
$ 2.79	Gallo (Gallo)
$ 2.99	United Vintners (Lejon)
$ 3.10	Almaden (Le Domaine)
$ 3.49	United (Lejon Blanc de Blancs)
$ 4.55	Christian Brothers
$ 4.99	Paul Masson
	Taylor (Great Western) [79]
$ 5.25	Almaden
$ 6.00	Beaulieu
$ 6.50	United Vintners (Inglenook)

$ 7.00	Beaulieu (Private Reserve)
$11.25	Mumms (Extra Dry) (Imported)
$14.65	Mumms (Cordon Rouge) (Imported)

(Prices are per fifth bottle at retail in 1974 in California)

396. Dr. Richard Courtney, an economist, is Vice President and Senior Economist at the Bank of America (Tr. 5435). He is an expert on consumer demand theory, the rationale behind consumer purchasing decisions and the way in which consumer purchasing decisions are translated into market demand functions (Tr. 6024, 6025).

397. As testified to by Dr. Courtney, a most significant factor in determining whether products are in competition with one another is substitutability as viewed by buyers (Tr. 5992–99). If a wine purchaser can buy wine over a range of prices, products within that range are viewed as substitutes for one another. And the products in that price range are in competition with one another (Tr. 5995).

398. The likelihood of individual consumers substituting wines of differing prices is greater if wines are sold over a range or spectrum of prices rather than at distinctly separate price points. The difference in price of a few cents is not likely to inhibit the consumer from substituting one wine for another (Tr. 5994, 5995). This is particularly true of frequently purchased, relatively low priced products such as wines, as opposed to high priced products such as automobiles, houses or television sets (Tr. 10,376). As found above, table wines, dessert wines and sparkling wines are each offered in a spectrum of a multitude of prices with closely spaced intervals.

399. Individual consumers and groups of consumers are more likely to substitute products from various producers as the number of alternatively priced products are increased and the price difference among products decreases (Tr. 5996–97). Many of the major low priced wine producers have expanded their product lines into a higher price range. Other major producers of high priced wines have extended their product lines into a lower price range (Findings 301–06, *supra*).

400. As wine prices do not invariably reflect their quality, there is a range of prices for wines of comparable quality. Wines of differing prices are thus substitutes for one another in terms of quality (Tr. 5997–98). [80]

401. To the extent consumers trade up over time to higher priced or higher quality wines, they are considering a wider range of alternatives (Tr. 5998–99). Trading up indicates that consumers view a broader range of alternative products as substitutes (Tr. 5998–99).

This is particularly true when substitution is viewed over a period of time (Tr. 5998–99).

402. The very considerations involved when a purchaser is determining whether to trade up from the so-called "standard" category to the "premium" category places all of the wines being judged in direct competition (Tr. 5998–99).

403. As consumers buy wines at different prices, they increase their knowledge about wines and broaden the range of wines which they consider acceptable substitutes. Consumers generally learn to appreciate drier and more complex wines as they gain experience and knowledge of wines (Tr. 768, 2849).

404. The availability of wines of various types and prices in a store or restaurant has an effect on the consumer's ability and inclination to substitute among them. A store or restaurant offering a wide selection of wine will allow a customer more substitutes among a broader range of wines (Tr. 5997).

405. Consumers have a range of choices in wine price and quality and the various wines from which they choose are in competition with one another (Tr. 788–89, 2868).

2. Submarkets—Table, Dessert, and Sparkling Wine

Production

406. In table wine production, grapes are delivered to the winery and crushed by mechanical crusher. The crushed grapes and their juice (called "must") are pumped into fermenting vats or tanks where fermentation takes place (CX 308V). In the process of fermentation, the grape sugar is converted to alcohol and the finished product is wine (Tr. 3130). Complete natural fermentation of grapes generally results in an alcohol content of 10 to 14 percent. Rarely does natural fermentation result in wines over 14 percent in alcohol (CX 308V). The use of 14 percent as a breaking point between tax categories for wine is because of this natural alcoholic level of wine (Tr. 1580–81). Fermentation takes from a few days to several weeks (CX 308V). Clarification of the liquid is done either before or after fermentation for white wines, and after fermentation for red wines. After fermentation, wines are aged (Tr. 3133–34, 3142–43). There are variations in length of aging, types of containers in which wines are aged and size of aging containers (Tr. 3133–34, 3139–40, 3142, 3143). Most wines are then blended to attain desired characteristics (CX 308Y). The wine is then bottled [81]and some wines are aged further in the bottle before shipment (CX 308Z–1).

407. The production of dessert wines (including appetizer wines

and vermouth) is essentially the same as for table wines through the fermentation process. Additional steps are required after fermentation, however. Dessert wines must be fortified to reach the desired over 14 percent level of alcohol. Fortification is accomplished by the addition of distilled alcohol from another source (Tr. 3154–55). Dessert wines are generally made with at least 17 percent alcohol to prevent spoilage (Tr. 3153–54). Fortification stops the fermentation process. The wine is then clarified and may be aged before being bottled. In the case of most sherries, the wine is generally baked (aged at high temperature) and clarified. It may then be aged or immediately bottled (Tr. 3158–59). Vermouths are flavored with herbs after fortification, following which they are clarified, aged for a short time and then bottled.

408. Sparkling wines are basically table wines with additional production steps to add the sparkle (Tr. 919). Sparkling wines are made from still (nonsparkling) white table wines. Sugar and yeast are added to the still wine in a closed container. The wine then undergoes a second fermentation, creating carbon dioxide which is not allowed to escape (Tr. 3170–71). This second fermentation can be done in a large (1,000–24,000 gallon) tank or in fifth gallon containers. If done in a tank the wine after fermentation is filtered in the tank to remove the yeast, bottled under pressure and then sold. If the second fermentation is done in bottles the wine may be transferred under pressure to a tank for filtering of the yeast. It is then rebottled and sold. This is called the "transfer process". Another method of removing yeast from the bottle involves keeping the bottles turned on end to allow yeast to settle in the neck of the bottle. The yeast is removed by freezing the bottle neck, removing the cap and allowing the frozen yeast to pop out. The bottle is then topped off, resealed and sold (Tr. 3171–74). This is called the "bottle process". Carbon dioxide can also be added to wine by artificial carbonation. There are not many carbonated wines on the market (Tr. 3170).

409. In the production of all wines there are many decisions made by the winemaker and many variations in the production process which cause variations in the resulting wines. As explained by Dr. Amerine, one of the leading authorities in viticulture and enology, "There are thousands of variations, almost as many as there are winemakers, time, temperature, procedures, when the procedures are applied, all of which to a smaller or larger extent will affect the gradation and quality of the wine" (Tr. 3153). [82]

410. The production of dessert wines requires equipment in

addition to that needed for table wines, including fortification tanks and a still to make alcohol for fortification (Tr. 529).

411. Production of sparkling wines requires specialized equipment not needed for table wines. Sparkling wines require pressure-resistant tanks to withstand the high pressure generated in the tank process or in the transfer process (Tr. 926, 3171–72). Pressurized bottling equipment and special corking equipment is needed. More expensive pressure resistant bottles, more expensive thicker corks and wire to hold the corks on are also required (Tr. 530, 923–24; CX 308Z–3).

412. Special handling is required for sparkling wines because of the hazards from pressurized bottles. Workers use gloves, face shields and protective aprons in handling sparkling wines (CX 308Z–4; Tr. 531).

Physical Differences

413. There are many differences in chemical composition (besides alcohol content) between table and dessert wines (Tr. 3168).

414. Table wines deteriorate soon after they are opened, while dessert wines, because of their higher alcoholic content, do not (Tr. 2846).

415. Sparkling wines lose their quality soon after opening (Tr. 2846).

416. Sparkling and carbonated wines contain a minimum level of carbon dioxide specified by government regulation (Tr. 3113, 3170; 26 U.S.C. 5041(a)). Thus, by legal requirement, they are different.

Differences in Use

417. As testified to by wine expert and columnist, Robert Balzer, "Even in relatively unsophisticated consumers there is the recognition that there are differences in wine and they fall into categories of table wine, appetizer and dessert wines, sparkling wines. Each one nominates itself for a different kind of use" (Tr. 2843–44).

418. Table wine, historically, is a fundamental and basic commodity and is the most important category (Tr. 2844). Table wines are generally served with a meal (Tr. 2844; CX 308D). Red, white and rose wines are each generally thought to go best with certain foods (CX 308N thru P).

419. Dessert wines (including appetizer wines) are generally used before or after a meal. The term "dessert wines" refers to wines over 14 percent in alcohol whether drunk as an appetizer or with dessert (Tr. 3153; CX 308L). [83]The main appetizer wines are sherry (except

cream sherries) and vermouth (CX 308M). Wines served with dessert include port, muscatel and tokay (CX 308 O). Cream sherries are sweet and are therefore generally drunk after dinner with dessert (CX 308M).

420. Sparkling wines are generally associated with festive uses or special occasions (Tr. 2845, 4884, 6290).

Consumer Recognition

421. Consumers generally recognize and understand the differences among table, dessert and sparkling wines. They are generally familiar with the names of common table wines as distinguished from the names of common dessert wines (Tr. 814, 2846–47).

422. Consumers are able to determine from the appearance of the bottle whether a wine is a sparkling wine as distinguished from either table or dessert wine. Sparkling wines are packaged in relatively thick bottles which have a different shape from bottles used for table and dessert wines. The appearance of the closure is also distinctive for sparkling wines (Tr. 814–16).

423. Dessert wines are frequently labeled "dessert wine." It is not unusual for table wines to be labeled "table wine" (Tr. 814).

Government and Industry Recognition

424. The wine industry recognizes three basic categories of wine which are commonly called table, dessert and sparkling wines (Tr. 1579–80, 1811–A). Still wines not over 14 percent alcohol are called "table wines". Still wines over 14 percent alcohol are called "dessert wines". Effervescent wines are called "sparkling wines" (Tr. 1579–80, 1811–A, 4107–08). Flavored wines are called "special natural" wines (26 U.S.C. 5386(a); CX 309K).

425. Table wines: All still wines not over 14 percent alcohol are taxed at $.17 per gallon (26 U.S.C. 5041(b)(i): CX 363; Tr. 4106). This category includes those flavored ("special natural") still wines not over 14 percent in alcohol such as Sangria and "refreshment wines" (26 U.S.C. 5041(o)(1); CX 363).

426. Dessert wines: All still wines over 14 percent alcohol, with one exception, are taxed at $.67 per gallon (26 U.S.C. 5041(b)(2); CX 363; Tr. 4107). This category includes those flavored ("special natural") still wines over 14 percent in alcohol, such as vermouth (26 U.S.C. 5041(b)(2); CX 309K, 363). The one exception is wines between 21 percent [84]and 24 percent alcohol which are used for blending only and are not commonly sold to the public (Tr. 4107–08).

427. Sparkling wines: Effervescent wines include "sparkling

wines" taxed at $3.40 per gallon and "artificially carbonated wines" taxed at $2.40 per gallon (CX 309J, 363). Artifically carbonated wines are a small part of the market (Tr. 3170). They include flavored ("special natural") effervescent wines (CX 309J, 363). Although artificially carbonated wines are taxed at a different rate, they are generally considered to be "sparkling wines" (Tr. 3170). The Wine Institute statistical tables have no separate category for carbonated wines, but include them with sparkling wines (CX 297A).

428. State taxes on wines also use the same three basic categories (CX 379R; Tr. 1578–80). In all but two states, the tax rates on carbonated and sparkling wines are the same. In all but one state, the tax rate on vermouth and other dessert wines are the same (CX 379R; Tr. 1579–80).

429. Table, sparkling and dessert wines are the three basic categories recognized by the wine industry. Industry witnesses categorized wine products in these three general categories (Tr. 617, 620, 919, 4192–93, 7422, 7424, 7592–93).

430. Table, sparkling and dessert wines are the basic categories utilized in reports on the wine industry's activities and trends. The *Wine Marketing Handbook,* described as the "industry bible" by a former vice president of marketing of United, reported wine sales for all wines and the three basic categories plus vermouth (Tr. 3669, 3733; CX 379U). The Bank of America, in a report on the wine industry, reported wine shipments in these three basic categories together with "all wine" (CX 288I–K).

431. United's former president, Bruno C. Solari, testified to the shift in the wine industry from dessert wines to table wines (Tr. 4756). Another former president of United, Richard Oster, testified to the growth of the "table wine market" in contrast to the decline in the "dessert wine market" (Tr. 7778, 7886, 8005). Bruce Johnson, former marketing vice president of United and former Heublein group product manager, testified to United's share of the "dessert wine market" (Tr. 3669, 3754–55).

432. Heublein's marketing strategy for its Vinya wine was intended to "capitalize on the expanding still table wine market" (CX 352N).

433. The McKinsey study of United and the wine industry, in addition to analyzing the wine industry as a whole, reviewed the consumption of wines in the three basic categories, table, dessert and sparkling wines (CX 220K). [85]

434. Louis Gomberg, Heublein's wine industry consultant, reported to Heublein in 1968 United's market shares in the three basic categories of table, dessert and sparkling wines (CX 206A; Tr. 1407).

435. John Powers, Chairman of the Board of United, continually monitors the shipments of United's competitors by using the gallonage figures reported by the California Board of Equalization. "They are an important part of our marketing intelligence" (Tr. 9485). Those gallonage figures are reported in the categories: wines not over 14 percent alcohol, wines over 14 percent alcohol and sparkling wines (Tr. 9696–97). The categories are not subdivided into "standard" or "premium" (Tr. 9695–97). Mr. Powers recognized that Jacare, which now is not carbonated, is a table wine, but when carbonated, was sold in the "sparkling wine market" (Tr. 9977–78).

436. Heublein has recognized the existence of the table, dessert and sparkling wine markets. In a voluntary submission to the Federal Trade Commission staff, Heublein recited the market shares of United in the table, dessert and sparkling wine markets (CX 327A, P, U, V).

437. The differential between the tax rates for table wines ($.17 per gallon) and sparkling wines ($3.40 per gallon) requires that the pricing structure for sparkling wines be higher than for table wines, with a resultant trend toward usage of sparkling wines for special occasions (CX 367T).

3. Exclusion of Refreshment Wines from Table Wine Submarket

438. While, because of their alcoholic content, they are taxed as still wines not over 14 percent, refreshment wines belong in a category separate and apart from other still wines not over 14 percent. This is due to differences in production, in the consumers to whom they appeal, in the uses to which they are put, in the manner in which they are marketed, and in their growth rates and life cycles. They are recognized within and without the industry as constituting a distinct category of wines (CX 53 O, 241E, 247D; RX 345–48).

439. Refreshment wines, also referred to as "pop" wines, are beverages generally much lower in alcoholic content (6–8 percent) than table wines (normally 10–14 percent; CX 308V). They are derived from fermentation of the cheapest available fruit concentrate, either apples, pears, grapes or other citrus fruits. Regardless of the fruit used to produce the alcohol, the resulting wine is "neutralized" or stripped of color and taste. Thereafter, the flavor, sweetener and character of the wine are added (Tr. 429–31, 566–67, 5144, 6179, 9534–36). As the former assistant production manager of Gallo explained: [86]

Well, the idea is that you strip the wine clean, more or less free from all flavor, by

doing it in a carbon column or ionic machine or some other method, and then you have what amounts to alcohol and water, but it is legally wine, and then you simply add flavor and sugars so that it is palatable and sell it as, with a proprietary name, and that is pop wine (Tr. 430).

440. The bulk of refreshment wine has been produced by Gallo under brands such as Boone's Farm, Ripple and Spanada; by United under brands such as Bali Hai, Annie Green Springs and T.J. Swann; and by Mogen David under the Cold Bear, Black Bear and JUG brands (CX 359L; RX 933K; Tr. 5155, 6181, 7353, 7797–98, 7822–24, 7911–13, 8308–09, 8319–21, 9535).

441. High-speed bottling lines used in the production of refreshment wines cannot be converted to the making of table wine (Tr. 9902). The former executive vice president of Pop Wines, Inc., a company created to specialize in pop wines, testified that Gallo's refreshment wines were competitive with his products but that the wines of other named producers of table wines were not (Tr. 5213–15). The marketing strategies applicable to refreshment wines are completely different from those applicable to dry table wines, even though both are still wines not over 14 percent (Tr. 7353–55, 8006–07, 8305–08, 8319–21, 9536).

442. Refreshment wines are consumed primarily by two segments of the population: young, college-age whites and urban blacks. United's T.J. Swann line, originally marketed to the college-age white consumer, was later repositioned and targeted towards urban blacks when market research showed they were responding to its taste and other characteristics. Many of the young consumers of refreshment wines desire their "soda pop" taste (RX 345B; Tr. 3768–69, 5214–15, 5239–41, 6182, 7796–98, 8319–21, 8362–66, 8555–56, 9535–36, 9978). Refreshment wines are frequently the first type of wine experienced by those who previously had been drinking beer and other non-wine, party-type beverages (Tr. 3768–69, 6182, 7353–55, 8319–20, 9534–36).

443. Consumers generally use refreshment wines for purposes distinct from those applicable to dry table wines. Whereas dry table wines are used primarily as an accompaniment to food at meals, refreshment wines are not so intended and are rarely consumed with meals. Refreshment wines are consumed as social beverages. Consumers who buy refreshment wines are interested in their flavor, palatability and refreshing qualities. Refreshment wines are generally served cold and over ice. They are not normally even promoted as being consumed in wine glasses (RX 345–48; Tr. 8319–20, 9535–36). [87]

444. Due to their refreshing nature and their appeal to youth,

refreshment wine sales have a distinctive seasonal pattern. Monthly shipments of dry table wines to wholesalers are generally even during most of the year, peaking at holidays; refreshment wines have peaks in the warm weather season beginning in April or May and have a major upsurge during the summer period (Tr. 9950).

445. Because refreshment wines are largely consumed at social gatherings of young adults, the major competitive products are soda pop and beer. A former Olympia Brewing Company executive said that his company regarded refreshment wines as competing with beer for the young adult trade. The former executive vice president of Pop Wines, Inc., explained: "The pop wines . . . are seen really as a mid-point, say, between the soda pop business and the beer business. It was essentially a soda pop with an alcoholic content" (Tr. 5214, 6179–81, 8319–21).

446. Refreshment wines are also distinguished from dry table wines by their placement in retail stores. Refreshment wines are shelved together with soft drinks and beer, in a refrigerated area apart from the retail space devoted to dry table wines (RX 347; Tr. 6181, 6607).

447. Sales of refreshment wines are characterized by extreme volatility. In contrast to dry table wines, the life cycles of these wine brands tend to be short, with accelerating sales increases and often with equally rapid declines (CX 53 O).

448. There has been a boom and bust cycle in the sales of refreshment wines. Refreshment wines happened very suddenly (Tr. 566–67). A peak year for refreshment wine sales was 1972 (Tr. 5209–11). From 1967–1972, refreshment wine shipments grew 2,185 percent from a relatively insignificant 2.8 million gallons to more than 64 million gallons. In the same period, shipments of table wines (exclusive of refreshment wines) grew from 85 million gallons to almost 156 million gallons or 83.5 percent.[18] [88]

4. Inclusion of Refreshment Wines in All Wine Market

HUV (RR 125–30; RRPF 148–50) contend that refreshment wines should be eliminated from the All Wine universe as well as from the share of each company in that category. To the contrary, the very evidence above relied upon to exclude refreshment wines from the

[18] The figures for refreshment wine shipments come from RX 15 and 27. The figures for table wines are derived by subtracting the refreshment wine gallonage as shown on RX 15 and 27 from CX 373V thru Z–7 (which include refreshment wine gallonage).

HUV's witness John Powers, Chairman of United, provided United sales figures for refreshment wine (Tr. 9539–40) which are inconsistent with those shown on RX 15. Since RX 15 was prepared as a statistical document for introduction into evidence, was introduced at the very beginning of HUV's defense (Tr. 6058) and the accuracy of the exhibit has never been challenged by any party, I am accepting RX 15 over the testimony of Mr. Powers.

table wine submarket demonstrates that they are properly considered in the broader all wine category.

449. Refreshment wines are fermented and made like other wines up to the point the different processes are followed. They are wines to which flavor has been added (CX 309Z–15). Gallo and United, the dominant companies in the production of all wines are also the dominant producers of refreshment wines and United produces its refreshment wines at the same facilities at which it produces table wines (CX 373; RX 15, 27; Tr. 9901). The winery in which Pop Wines, a company which entered to make only refreshment wines, operated was a bulk winery that had been in existence for 30 to 40 years (Tr. 5134, 5136).

450. Wine, in general, not merely refreshment wine, is recognized by the Wine Institute (the wine industry trade association) as appropriate for use in mixed wine coolers for summer, hot drinks in winter and punches for parties all year around (CX 308G). Table wine use is not limited to meals, and white wines in particular are increasingly being utilized as cocktails (Tr. 7685; CX 367Z–10 thru Z–13).

451. Refreshment wines are viewed as an introductory wine to accustom young consumers to wine drinking with the expectation that they will then develop a taste for better quality table wines (Tr. 5281; CX 53 O). Heublein and United direct promotions of Lejon, Inglenook, Faisca and Lancers wines to young consumers and to ages just older than college level (CX 116N, 129C, 256Z–57, 65).

452. Refreshment wines are sold through the same channels of distribution as all other wines (Tr. 3310–11; CX 218Z–280, Z–281, Z–292, Z–293, Z–295, 256Z–34, Z–38, 371). An effort is made to have white and rose wines placed in the cold box of retailers (Tr. 6609).

453. In summary, while there are differences sufficient to require the exclusion of refreshment wines from the table wine submarket, refreshment wines clearly are properly included in the overall all wine market. [89]

Discussion of Applicable Law and Conclusion

"All Wines" constitute the relevant product market. The following summarizes the application of the criteria enunciated in *Brown Shoe Co.* v. *U.S.*, 370 U.S. 294 (1962):

1) All wines share certain physical characteristics unique to wine and are used for the same general purposes. All wines are products of the fermented juice of grapes or other fruits; and, as alcoholic

beverages distinct from others, their principle use is as articles of food.

2) All wines are produced from similar raw materials, by similar production processes, using similar production expertise. While different varieties of grapes or other fruits may be used to produce different varieties of wine, and while additional steps may be added to the basic production process to produce dessert or sparkling wine, all wines are produced by the basic process of crushing, fermenting, clarification and bottling. Individual wineries are capable of using different varieties of raw materials and of changing their product line and quality.

3) Federal and state governments, as well as the wine industry itself, view the wine industry as a single group. Federal and state regulations (except for different tax rates on table, dessert and sparkling wines) on entry, tax bonding, distribution and retail pricing procedures are common for all wines. Industry trade associations, such as the Wine Institute (the primary trade group), and professional associations such as the American Society of Enologists, include representatives of producers of all wines.

4) All wines are distributed through the same wholesale and retail distribution channels, and are thus in competition with one another for wholesale distribution and retail shelf space.

5) Consumer purchasing patterns indicate public recognition of all wines as being in competition with one another, although consumers may choose particular wines for particular occasions. [90]

While complaint counsel have not shown that price sensitivity[19] exists throughout the all wines market, price sensitivity alone is not determinative of the existence or non-existence of a product market. In *U.S.* v. *Continental Can Co.*, 378 U.S. 441 (1964), the Court held:

> . . . price is only one factor in a user's choice between one [product] or another. That there are price differentials between the two products or that the demand for one is not particularly or immediately responsive to changes in the price of the other are relevant matters but not determinative of the product market issue (at 455).

HUV argue that, since there was a great disparity in retail prices between the products sold in 1969 by Heublein (primarily Lancers at $3.98 and Harveys Bristol Cream at $7.79) and United (the majority of whose products sold for less than $1.50), there was no actual competition between Heublein and United. They contend that " . . . the alleged markets aggregate competitively distinct products and

[19] An additional *Brown Shoe* criterion.

thereby ignore the very competitive realities relevant market determinations are intended and required to honor" (RPF 178).

This position is without merit. " . . . [I]t is improper 'to require that products be fungible to be considered in the relevant market,' *United States* v. *duPont,* 351 U.S. 377, 394," *U.S.* v. *Continental Can Co., supra,* at 449. And, in *Telex Corp.* v. *International Business Machine Corp.,* 510 F.2d 894 (10th Cir. 1975), the court found:

> One evidence of cross-elasticity is the responsiveness of sales of one product to price changes of another. But a finding of actual fungibility is not necessary to a conclusion that products have potential substitutability (at 917–18).

As complaint counsel's economic expert witness, Dr. Richard Courtney, testified (Tr. 5992–93, 5995–96, 6027), interchangeability in use is an accepted measure of substitutability, and products capable of being utilized for the same purpose are substitutes, and thus in competition. All wines, regardless of price, variety, or production method, are capable of consumption as alcoholic beverage food products, and are thus in competition with one another.

HUV rely on *United States* v. *The Federal Company,* 403 F. Supp. 161 (W.D. Tenn. 1975), for the proposition that "when manufacturers of apparently similar products consistently fail to react to each other's price changes, this shows that [91]they do not perceive the products as competitive and that the products do not, in fact, compete" (RPF 224). In that case, the court found that all wheat flours, including family flour, bakery flour, ingredient flour, industrial flour, durham flour and mill feed are not one line of commerce. The court determined that the various products derived from the wheat milling process have different physical compositions and are not substitutes for one another. They are sold at different prices to different customers for different uses and there is not a fixed relationship in price among them; that there are different pricing systems for family flour and bakery flour; and, that each product is usually sold by different personnel. The case, therefore, does not support HUV's position.

Complaint counsel's proposed submarkets, table, dessert and sparkling wines, are also appropriate. The same criteria enunciated in *Brown Shoe,* 370 U.S. 294, support these submarkets. As discussed in the factual findings above, table wines (still wines not over 14 percent alcohol by volume), dessert wines (still wines over 14 percent alcohol by volume) and sparkling wines have distinct physical characteristics (*e.g.,* alcohol content), distinct additional production processes (*e.g.,* fortification or addition of carbonation), distinct uses (*e.g.,* consumption with meal or as aperitif or after-dinner drink),

and distinct consumer recognition (*i.e.*, table wine is often referred to as "dinner" wine, champagne is for "special occasions", Tr. 2845, 6290; Heublein's advertising campaign for Harveys Bristol Cream as an after-dinner drink: "Never serve the coffee without the Cream" (CX 97Z-6)).

HUV argue that the proper submarkets should be "standard" and "premium" wines, asserting that there is no competition between these categories, and the industry and public recognizes such a distinction. This position is not supported by the evidence of record in this proceeding and is legally untenable. Despite extensive pleadings, HUV have not shown where clear demarcations in price, packaging, advertising, production, distribution or consumer purchasing patterns are found to support their proposed submarkets. Indeed, the facts of record show just the opposite of what HUV contend. A broad spectrum of prices is apparent among wines, all of which are clearly substitutable in end use. The Court in *Brown Shoe, supra,* reached the same conclusion as that reached here in refusing to hold that " . . . medium-priced shoes do not compete with low-priced shoes . . . It would be unrealistic to accept Brown's contention that, for example, men's shoes selling below $8.99 are in a different product market from those selling above $9.00" (at 326). In *U.S.* v. *Joseph Schlitz Brewing Co.,* 253 F. Supp. 129 (N.D. Cal., 1966), the court found, "There are no distinguishable price levels [92]of beer which constitute relevant product submarkets within the line of commerce found by the court" (at 143). Also, in *Mogul* v. *General Motors Corporation,* 391 F. Supp. 1305 (E.D. Pa., 1975), the court took judicial notice of the fact that:

> . . . the relevant product market cannot be limited to Cadillac. The Cadillac . . . competes with even the less expensive models of automobiles in serving the consuming public's transportation needs and desires (at 1313).

Respondents' own economist witness, Dr. Irstin Barnes, testified that for products subject to frequent purchase, such as foods and beverages, products with different prices do tend to be regarded by consumers as substitutes for one another (Tr. 10,376). He agreed with the proposition that: "To the extent you increase the difference in price between two products, the price overcomes the difference in quality" (Tr. 10,402), thus enhancing competition between the differently priced products.

The Commission has held, with respect to dog food, that "to be sure, the differing price and quality grades demonstrated by respondents do support finding separate submarkets here, but the submarkets are closely associated in one market," *Liggett & Myers,*

Inc., Docket 8938, 87 F.T.C. 1074, at 1158 (1976). Although there may be some recognition of grades of qualities of wine usually referred to a "standard" and "premium", precise demarcation is not possible. A Wine Institute publication, *The Story of Wines,* explains that:

> Wine, because it continually changes in quality even after bottling, and because its desirable characteristics defy measurement, has never had an industry-wide quality grading system such as many other products have. Individual vintners have their own grading systems, but these are not uniform between companies. Some vintners have low-priced and higher-priced brands; others use vintage dates or such words as "special", "deluxe", "select", "reserve", or "private stock" to denote quality differences (CX 308Z–6).

As the Commission recently stated in *Coca-Cola Bottling Company of New York, Inc.* (Docket 8992, January 23, 1979):

> The principles governing antitrust market definition are designed to satisfy the necessity to make difficult judgments in an area of unavoidably imperfect knowledge, and markets so designated cannot always (nor need they, as a matter of law) satisfy the purist's [93]desire that every product within them possess a high degree of cross-elasticity of demand with every other (at 10).

Brown Shoe and the cases following it recognize that any reasonably proved submarket may support a finding of illegality. In *U.S.* v. *Mrs. Smith's Pie Co.,* 440 F. Supp. 220 (E.D. Pa., 1976), the court held that "Since the Clayton Act is concerned with *any* [*sic*] line of commerce, the government need not base its case on the narrowest possible market . . . However, nothing . . . precludes use of a narrower product market if that is the 'line of commerce' where competition is affected" (at 229).

Accordingly, even if narrower product markets such as "standard" and "premium" could have been established, this would not have precluded the appraisal of the effects of the acquisition on the broader "all wines" market and the "table", "dessert" and "sparkling" wine submarkets.

454. Based upon the foregoing findings of fact and in consideration of the applicable law, the relevant product market within which to appraise the effects of the acquisition is found to be all wines (domestic and imported); and the appropriate submarkets are table wines (excluding refreshment wines), dessert wines and sparkling wines.

VI. STRUCTURE OF WINE INDUSTRY AND RELEVANT ACTIVITIES

455. Both domestic and foreign wines are marketed in the United States (CX 218A thru Z–316, 366A thru Z–22).

456.. Shipments into distribution channels refer to tax-paid

withdrawals of wine together with imports of wine for consumption. Tax-paid withdrawals of wine are withdrawals from bonded status at which time state and federal taxes are assessed. Normally, wines remain in bonded status until they are ready for market (CX 295L; Tr. 4039–42).

A. Shipments

1. All Wines

457. In 1960, shipments of all commercially produced wine entering distribution channels in the United States totaled 163,352,000 gallons. In 1968, all wine shipments had increased to 213,658,000 gallons. In 1976, all wine shipments had grown to 376,389,000 gallons (CX 273, 295J, 366I, 373E; Wine Institute Bulletin, March 24, 1978, No. 78–3, Table 2, officially noticed September 27, 1978). [94]

458. From 1957 through 1966 shipments of all wines grew from 151,881,000 gallons of commercially produced wine entering distribution channels in the United States to 191,176,000 gallons, for an average annual growth rate of about 4.4 million gallons. Between 1966 and 1967, all wine shipments grew 12.2 million gallons. Thereafter, shipments of all wines grew substantially from year to year. Total shipments of all wine increased approximately:

Gallons (millions)	*Year*
10.3	1967 to 1968
22	1968 to 1969
31.7	1969 to 1970
37.9	1970 to 1971
32	1971 to 1972
10	1972 to 1973
2	1973 to 1974
18.6	1974 to 1975
8.4	1975 to 1976

Between 1966 and 1976, the all wine market grew at an average annual rate of approximately 18.5 million gallons (CX 295J, 366I, 373C, E, F, H, J, K; Wine Institute Bulletin, March 24, 1978, No. 78–3, Table 2, officially noticed September 27, 1978).

2. Table Wines[20]

459. From 1968 through 1972, table wine shipments including all still wines not over 14 percent alcohol by volume (excluding refreshment wines) entering distribution channels in the United States grew substantially from year to year. Table wine shipments grew by approximately:

Gallons (millions)	*Year*
12.2	1968 to 1969
14.7	1969 to 1970
13.5	1970 to 1971
22.0	1971 to 1972

(CX 295J, 373Z, Z–2, Z–4, Z–6, Z–7; RX 15A–B, 27A–B).

In 1968, table wine shipments entering distribution channels in the United States, amounted to 93,445,400 gallons and constituted 43.7 percent of all commercially produced wines entering distribution channels in the United States (CX 295J; RX 15A–B, 27A–B). [95]

3. Refreshment Wines

460. In 1968, refreshment wines entering distribution channels in the United States amounted to 5,321,000 gallons and constituted 2.5 percent of all commercially produced wines entering distribution channels in the United States (RX 15A–B, 27A–B). In 1972, their share had increased to 19 percent (CX 373K).

461. Between 1968 and 1972, refreshment wines entering distribution channels in the United States grew dramatically. Shipments were approximately:

Year	*Gallons (millions)*
1968	5.3
1969	14.3
1970	29.9
1971	51.7
1972	64.3

(RX 15A–B, 27A–B)

[20] In view of the exclusion of refreshment wines from the table wine market, and there being no record evidence of refreshment wine shipments subsequent to 1972, findings on the table wine market do not go beyond 1972.

4. Dessert Wines

462. Between 1957 and 1967, the volume of dessert wines entering distribution channels in the United States has fallen and risen but overall has shown a decline. Since 1968, dessert wine shipments (including vermouth and other special natural still wines over 14 percent alcohol by volume) have continued to decline from 102,377,600 gallons in 1968 to 94,566,000 gallons in 1976 (CX 273U, 295J; Wine Institute Bulletin, March 24, 1978, No. 78–3, Table 2, officially noticed September 27, 1978).

463. In 1968, domestic and imported dessert wines (including vermouth and other special natural still wines over 14 percent alcohol by volume) were the largest selling wine type, accounting for 47.9 percent of all commercially produced wine entering distribution channels in the United States (CX 295J, 373E, N).

464. In 1976, dessert wine shipments declined to 21 percent of all wine shipments entering distribution channels in the United States (Wine Institute Bulletin, March 24, 1978, No. 78–3, Table 2, officially noticed September 27, 1978).

5. Sparkling Wines

465. In 1960, shipments of commercially produced sparkling wine entering distribution channels in the United States totaled 4,321,000 gallons, accounting for 2.6 percent of all wine shipments. In 1968, sparkling wine shipments had grown to 12,513,000 gallons or 5.9 percent of all wine shipments entering distribution channels in the United States (CX 295J). [96]

466. Shipments of sparkling wine peaked in 1971, totaling 23,970,000 gallons, or 7.8 percent of all wine shipments (CX 295J, 373J, Z–12).

467. From 1971 through 1976, sparkling wine shipments entering distribution channels in the United States have declined and leveled off, ranging between 20 and 22 million gallons annually. In 1976, shipments of sparkling wines were 21.8 million gallons, or 5.8 percent of total wine shipments entering distribution channels in the United States (CX 366I).

468. After increasing over 500 percent between 1960 and 1971, sparkling wine shipments went into a period of decline as cold duck sales collapsed. The sparkling wine shipment decline leveled out in 1975 and in 1976 sparkling wine shipments grew 7 percent over 1975 shipments (CX 366T).

B. Concentration and Concentration Trends

469. The four firm concentration ratio of the all wine market in the United States was 47.4 percent in 1967, 47.9 percent in 1968, 50.9 percent in 1969, 53.6 percent in 1970, 56.7 percent in 1971 and 54.6 percent in 1972 (CX 373B, D, F, H, J, K).

470. The eight firm concentration ratio of the all wine market in the United States was 55.9 percent in 1967, 57.4 percent in 1968, 60.3 percent in 1969, 63.6 percent in 1970, 67.0 percent in 1971 and 66.0 percent in 1972 (CX 373B, D, F, H, J, K).

471. The four firm concentration ratio of the United States table wine market, consisting of still wines not over 14 percent alcohol by volume (excluding refreshment wines), was 49.7 percent in 1967, 48.1 percent in 1968, 47.4 percent in 1969, 47.4 percent in 1970, 47.0 percent in 1971 and 43.5 percent in 1972 (CX 373V, Y, Z-2, Z-4, Z-6, Z-7; RX 15A-B, 27A-B).

472. The eight firm concentration ratio of the United States table wine market, consisting of still wines not over 14 percent alcohol by volume (excluding refreshment wines), was 61.0 percent in 1967, 60.0 percent in 1968, 59.6 percent in 1969, 60.5 percent in 1970, 59.4 percent in 1971 and 57.4 percent in 1972 (CX 373V, Y, Z-2, Z-4, Z-6, Z-7; RX 15A-B, 27A-B).

473. The four firm concentration ratio of the United States dessert wine market, consisting of still wines over 14 percent alcohol by volume, was 49.0 percent in 1967, 50.4 percent in 1968, 51.3 percent in 1969, 52.4 percent in 1970, 54.6 percent in 1971 and 52.4 percent in 1972 (CX 373L, N, P, R, T, U). [97]

474. The eight firm concentration ratio of the United States dessert wine market, consisting of still wines over 14 percent alcohol by volume, was 56.1 percent in 1967, 58.5 percent in 1968, 59.5 percent in 1969, 61.2 percent in 1970, 63.7 percent in 1971 and 63.5 percent in 1972 (CX 373L, N, P, R, T, U).

475. The four firm concentration ratio of the United States sparkling wine market was 37.0 percent in 1967, 41.9 percent in 1968, 54.9 percent in 1969,[21] 56.8 percent in 1970, 59.6 percent in 1971 and 61.0 percent in 1972 (CX 373Z-8 thru Z-13).

476. The eight firm concentration ratio of the United States sparkling wine market was 56.5 percent in 1967, 62.7 percent in 1968, 71.9 percent in 1969, 73.7 percent in 1970, 75.2 percent in 1971 and 78.0 percent in 1972 (CX 373Z-8 thru Z-13).

[21] Until November 1969, Lancers met the definition of and was taxed as a carbonated wine and thus fell within the sparkling wine submarket. In that month, Heublein stabilized the carbonation of Lancers at a level below that required of a carbonated wine, thus changing its position to that of a table wine (Tr. 8705-14). As of that time, Heublein could no longer market Lancers as an effervescent wine, whether by packaging, advertising or otherwise (CX 309Z-25). Statistics for 1969, however, do not reflect the change and include Lancers as a sparkling wine for the entire year.

477. These concentration ratios narrated above follow in tabular form:

ALL WINE MARKET SHARE

	Top 4	Top 8
1967	47.4%	55.9%
1968	47.9	57.4
1969	50.9	60.3
1970	53.6	63.6
1971	56.7	67.0
1972	54.6	66.0

TABLE WINE MARKET SHARE

	Top 4	Top 8
1967	49.7%	61.0%
1968	48.1	60.0
1969	47.4	59.6
1970	47.4	60.5
1971	47.0	59.4
1972	43.5	57.4 [98]

DESSERT WINE MARKET SHARE

	Top 4	Top 8
1967	49.0%	56.1%
1968	50.4	58.5
1969	51.3	59.5
1970	52.4	61.2
1971	54.6	63.7
1972	52.4	63.5

SPARKLING WINE MARKET SHARE

	Top 4	Top 8
1967	37.0%	56.5%
1968	41.9	62.7
1969	54.9	71.9

	Top 4	Top 8
1970	56.8	73.7
1971	59.6	75.2
1972	61.0	78.0

478. Professor Scherer has written that when 40 percent of a market is concentrated in the top four firms, inter-firm interdependence and coordination become increasingly probable. Professors Kaysen and Turner have found that when the top eight firms have 50 percent of the market, there is a Type 1 oligopoly where there is a great likelihood that the firms will recognize their interdependence and act in a non-competitive manner. They have classified as a tight oligopoly the situation where the top four firms have 50 percent (Tr. 5679–81). These are generally accepted benchmarks of a concentrated industry and are being applied in this case.

479. Measured both by four firm and eight firm concentration ratios, the all wine market and the table wine and dessert wine submarkets were concentrated in the period 1967 through 1972 (CX 373).

480. Measured by four firm concentration ratios, the sparkling wine submarket was concentrated in the period 1968 through 1972 (CX 373).

481. Measured by eight firm concentration ratios, the sparkling wine submarket was concentrated in the period 1967–1972 (CX 373).

482. Measured both by four firm and eight firm concentration ratios, the all wine market and the dessert and sparkling wine submarkets were characterized by increases in concentration over the period 1967 through 1972 (CX 373). [99]

483. Four firm and eight firm concentration ratios in the all wine market and in the table and dessert wine submarkets may be understated due to the inclusion of United States taxpaid withdrawals of all bulk wine in the universe figures for each market but exclusion of taxpaid withdrawals of bulk wine, except taxpaid withdrawals of bulk wine shipped to franchised bottlers, from individual firm shipments (CX 373A). There is no evidence that sparkling wines are, or can be, shipped in bulk form.

484. In 1968, the year before the merger, the all wine market eight firm concentration of 57.4 percent exceeded the 50 percent threshold at which Professors Kaysen and Turner deemed industry interfirm coordination and interdependence likely. In 1968, the all wine market four firm concentration of 47.9 percent exceeded the 40

percent threshold at which Professor Scherer deemed industry interfirm coordination likely (CX 373D; Tr. 5681, 5684–85).

485. In 1972, the all wine market four firm concentration of 54.6 percent exceeded the 50 percent threshold at which Professors Kaysen and Turner characterized an industry as a tight oligopoly within which interfirm coordination and interdependence is extremely likely (CX 373K; Tr. 5681–82).

486. In 1968, the United States table wine market was concentrated. By Professors Kaysen's and Turner's four firm concentration standards, in 1968, the table wine market approached tight oligopoly in which interfirm coordination and interdependence is extremely likely. The four firm concentration in this market in 1968 also exceeded the 40 percent threshold at which Professor Scherer deemed interfirm coordination and interdependence likely (CX 373Y; Tr. 5680–81, 5684). In 1972, the table wine market remained concentrated, exceeding Professor Scherer's 40 percent threshold (CX 373Z–7; Tr. 5681–82).

487. In 1968, the United States dessert wine market was concentrated. By Kaysen and Turner's, four firm concentration standards, in 1968, the dessert wine market qualified as a tight oligopoly in which interfirm coordination and interdependence is extremely likely to occur. The four firm concentration in this market in 1968 also exceeded the 40 percent threshold at which Professor Scherer deemed interfirm coordination and interdependence likely (CX 373N; Tr. 5681–82, 5687). In 1972, the dessert wine market remained a tight oligopoly by Kaysen and Turner's four firm concentration standards (CX 373U; Tr. 5681–82).

488. In 1968, the United States sparkling wine market was concentrated. The four firm concentration in this market in 1968 exceeded the 40 percent threshold at which Professor Scherer deemed interfirm coordination and [100]interdependence likely. In 1968, the eight firm concentration in this market exceeded the 50 percent threshold at which Professors Kaysen and Turner deemed interfirm coordination and interdependence likely (CX 373Z–9; Tr. 5680, 5686). In 1972, the sparkling wine market four firm concentration ratio exceeded the 50 percent threshold at which Professors Kaysen and Turner characterized a market as a tight oligopoly in which interfirm coordination and interdependence is extremely likely (CX 373Z–13; Tr. 5681–82).

489. No data beyond calendar year 1972 exists in the record of the share of the top four and top eight companies of the United States all wine market, measuring individual company shares by taxable withdrawals of bottled wine and of franchised bulk wine plus

imports for consumption. However, the record contains data beyond 1972 on wine shipments by the ten largest United States wineries.

490. Domestically produced wine of the ten largest United States wineries, as a percentage of total wine shipments entering distribution channels, measured by domestic taxable withdrawals of bottled wine and of all bulk wine plus imports for consumption, accounted for 71 percent of all wine shipments in 1973. The domestically produced wine of the ten largest United States wineries dropped to 68 percent of total wine shipments in 1974, recovered to 69 percent in 1975, and rose to 69.4 percent in 1976. Over the period 1970 through 1976, the share of the ten largest United States wineries increased from 66 percent to 69.4 percent of total wine shipments entering distribution channels in the United States (CX 366U–Z; see also CX 295J; Wine Institute Bulletin, March 24, 1978, No. 78–3, Table 2, officially noticed September 27, 1978, for universe figures).

491. In the all wine market, the four firm concentration ratio during the period 1973 through 1976 remained beyond the 50 percent threshold level at which Professors Kaysen and Turner considered the industry interfirm coordination and interdependence extremely likely to occur. The four largest United States wineries (Gallo, United Vintners, Almaden, and Mogen David/Franzia), not including their affiliated imported wine operations, alone accounted for 56 percent in 1973, 53 percent in 1974, 53 percent in 1975 and 53 percent in 1976 of the universe of all domestic and imported wine shipments entering distribution channels in the United States. The eight largest United States wineries (the four named above and Canandaiqua, Guild, Taylor and Monarch), not including their affiliated imported wine operations, alone accounted for 69 percent in 1973, 66 percent in 1974, 67 percent in 1975 and 66.8 percent in 1976 of the universe of all domestic and imported wine shipments entering distribution channels in the United States (CX 366Y–Z; Tr. 5681–82). **[101]**

492. Beyond calendar year 1972, no record data exists of the share of the top four and top eight firms in the dessert wine market measuring individual firm share by taxable withdrawals of bottled dessert wine and of franchised bulk dessert wine plus dessert wine imports for consumption. However, the record contains data with respect to dessert wine shipments by California producers.

493. In the period 1973 through 1976, the dessert wine market remained concentrated. The four largest California producers of dessert wines (Gallo, United Vintners, Guild and Bear Mountain), not including their affiliated imported wine operations, alone accounted for 50 percent in 1973, 45 percent in 1974, 48 percent in

1975 and 49.6 percent in 1976 of total domestic and imported shipments of dessert wines. Four firm concentration in the period 1973 through 1976 in the dessert wine market, measured by shipments of the top four California producers alone, exceeds the 40 percent threshold at which Professor Scherer deemed industry interfirm coordination and interdependence likely. The eight largest California producers of table wines (the four named above and Franzia, Christian Brothers, California Wine Association and Paul Masson), not including their affiliated imported wine operations, alone accounted for 60 percent in 1973, 53 percent in 1974, 56 percent in 1975 and 58.0 percent in 1976 of total shipments of domestic and imported dessert wines entering distribution channels in the United States. The eight firm concentration in the period 1973 through 1976 in the dessert wine market, measured by shipments of the top eight California producers alone, exceeds the 50 percent threshold at which Professors Kaysen and Turner consider industry interfirm coordination and interdependence likely to occur (CX 366Z–1; Tr. 5681–82).

494. Beyond calendar year 1972, no record data exists of the share of the top four and top eight firms in the United States sparkling wine market, measuring individual firm share by taxable withdrawals and franchised bulk wine (if any) plus imports for consumption. However, the record contains data beyond 1972 with respect to the share of the sparkling wine market held by the ten largest California wineries, not including their affiliated imported wine operations. As a percentage of the total universe of sparkling wine shipments entering distribution channels as measured by domestic taxable withdrawals of bottled sparkling wine and franchised bulk sparkling wine (if any) plus sparkling wine imports for consumption, the ten largest California sparkling wine producers, not including their affiliated imported wine operations, accounted for 68 percent in 1973, 70 percent in 1974, 72 percent in 1975 and 69.3 percent in 1976 of total shipments of sparkling wines entering distribution channels in the United States. Over the period 1970 through 1976, the share of the ten largest California sparkling wine producers increased from 59 percent to 69.3 percent of total domestic and imported sparkling wine [102]shipments entering distribution channels in the United States (CX 366Z–2; see also CX 295J; Wine Institute Bulletin, March 24, 1978, No. 78–3, Table 2, judicially noticed September 27, 1978, for universe figures).

495. In the sparkling wine market, the four firm concentration during the period 1973 through 1976 remained beyond the 50 percent threshold level at which Professors Kaysen and Turner consider

industry interfirm coordination and interdependence extremely likely. The four largest California producers of sparkling wines (Gallo, United Vintners, Almaden and Franzia), not including their affiliated imported wine operations, alone accounted for 58 percent in 1973, 57 percent in 1974, 56 percent in 1975 and 54.7 percent in 1976 of total shipments of domestic and imported sparkling wines entering distribution channels in the United States. The eight largest California producers of sparkling wines (the four named above and Paul Masson, Guild, Korbel and Weibel), not including their affiliated imported wine operations, alone accounted for 67 percent in 1973, 67 percent in 1974, 68 percent in 1975 and 66.2 percent in 1976 of total shipments of domestic and imported sparkling wines entering distribution channels in the United States (CX 366Z-2).

496. The all wine market and the table, dessert and sparkling wine submarkets were concentrated at the time of the merger and remained concentrated through 1972. And concentration increased during that period in the all wine market and in the dessert and sparkling wine submarkets. As further demonstrated above, in the period 1973 through 1976, the all wine market and the dessert and sparkling wine submarkets remained concentrated.[22]

The trends towards increasing concentration over the period 1967 through 1972 in the United States in the all wine market and in the dessert and sparkling wine submarkets increase the probability of recognized interdependence among wine producers and hence the probability of interfirm coordination. The effects of the merger, therefore, must be evaluated in the light of this concentrated state of the industry.

C. Skewness

497. In the period 1967 through 1972, the size distribution of market shares among the top four and top eight firms in the all wine market and in the table and dessert wine submarkets was skewed (Tr. 5699-5701). In the period 1969 through 1972, the size distribution of market shares among the [103]top four and top eight firms in the sparkling wine market was skewed (Tr. 5701). This skewness increases the probability of interfirm coordination among the competitors in the all wine market and the three submarkets (Tr. 5696-5701).

498. The size distribution of the market shares of firms within the top eight competitors in the United States all wine market in the

[22] There is no record evidence covering the post 1972 period for table wines excluding refreshment wines.

period 1967 through 1972 was as follows (CX 373D, F, H, J, K; Tr. 5698):

ALL WINE MARKET

	1967 % Market	*1968 % Market*	*1969 % Market*	*1970 % Market*	*1971 % Market*	*1972 % Market*
E. & J. Gallo Winery	22.9	24.0	25.8	29.2	32.7	32.4
United* Vintners, Inc.	18.7	17.9				
Heublein, Inc.			18.9	18.3	16.9	14.5
Schenley Industries, Inc.	2.9	3.0	3.1	3.2		
The Taylor Wine Co., Inc.	2.8	3.1	3.1	2.9	2.9	2.9
Joseph E. Seagram & Sons, Inc.	2.3	2.5	2.4	2.3	2.1	2.3
Mogen David Wine Corp.	2.1	2.5	2.2	2.5	2.9	3.6
Guild Wineries and Distilleries	2.0				3.9	3.8
National Distillers & Chemical Corp.	2.0	2.3	2.4	2.8	3.2	3.9
Franzia Bros. Winery		2.2	2.4	2.3	2.3	2.6

*Effective 1969, United's figures are included with Heublein's. [104]

499. The size distribution of the market shares of firms within the top eight competitors in the United States table wine market in the period 1967 through 1972 was as follows (CX 373V, Y, Z–2, Z–4, Z–6, Z–7; RX 15A–B, 27A–B):

TABLE WINE MARKET*

	1967 % Market	*1968 % Market*	*1969 % Market*	*1970 % Market*	*1971 % Market*	*1972 % Market*
E. & J. Gallo Winery	24.2	24.6	25.5	23.9	21.7	20.4
United** Vintners, Inc.	17.4	14.6				
Heublein, Inc.			13.7	14.6	14.1	12.5
Mogen David Wine Corp.	5	5.4	4.5	4.5	4.3	3.6
National Distillers & Chemical Corp.	3.1	3.5	3.8	4.5	5.7	7.0
Guild Wineries and Distilleries	3.1	2.9	2.9	3.2	5.5	5.2
Schenley Industries, Inc.	2.9	3.1	3.3	3.8		
Joseph E. Seagram & Sons, Inc.		2.9	2.7	2.7	2.5	3.1
Monarch Wine Co., Inc.	2.6				2.2	1.8
Franzia Bros. Winery	2.6	2.9	3.3	3.3	3.4	3.8

*Excluding refreshment wines.

**Effective 1969, United's figures are included with Heublein's. [105]

500. The size distribution of the market shares of firms within the top eight competitors in the United States dessert wine market in the period 1967 through 1972 was as follows (CX 373L, N, P, R, T, U):

DESSERT WINE MARKET

	1967 % Market	*1968 % Market*	*1969 % Market*	*1970 % Market*	*1971 % Market*	*1972 % Market*
E. & J. Gallo Winery	22.9	22.9	22.9	22.0	21.1	20.6
United* Vintners, Inc.	20.1	21.0				
Heublein, Inc.			21.2	22.5	24.6	22.7
Schenley Industries Inc.	3.0	3.2	3.5	3.8		
Taylor Wine Co., Inc.	2.9	3.3	3.8	4.1	4.6	4.7
Canandaigua Industries Co., Inc.	2.3	2.6	2.5	2.8	3.0	3.9
Joseph E. Seagram & Sons, Inc.	1.6	1.9	2.0	2.1	2.1	
California Wine Association	1.6	1.8	1.8			
Renfield Importers, Ltd.	1.6	1.7		2.1		2.4
The Christian Brothers			1.8	1.8	2.0	2.0
Mogen David Wine Corp.					2.0	2.8
Guild Wineries and Distilleries					4.3	4.4

*Effective 1969, United's figures are included with Heublein's. [106]

501. The size distribution of the market shares of firms within the top eight competitors in the United States sparkling wine market in the period 1967 through 1972 was as follows (CX 373Z–8 thru Z–13):

SPARKLING WINE MARKET

	1967 % Market	*1968 % Market*	*1969 % Market*	*1970 % Market*	*1971 % Market*	*1972 % Market*
E. & J. Gallo Winery		11.3	18.0	27.9	32.8	33.1
United* Vintners, Inc.	10.6	10.7				
Heublein, Inc.	6.0	7.2	20.9	16.4	15.0	14.5
The Taylor Wine Co., Inc.	14.1	12.7	10.5	7.3	6.9	7.6
Joseph E. Seagram & Sons, Inc.	6.4	6.0	4.6	4.2	4.0	4.5
National Distillers & Chemical Corp.	5.8	6.3	5.6	4.9	4.8	5.8
Monarch Wine Co., Inc.	4.6	4.6	4.9	5.2	4.6	4.2
Robin Fils & Cie., Ltd.	4.5	3.9	4.1	4.2	3.1	

*Effective 1969, United's figures are included with Heublein's. [107]

	1967 % *Market*	*1968* % *Market*	*1969* % *Market*	*1970* % *Market*	*1971* % *Market*	*1972* % *Market*
Weibel, Inc.	4.5					
Guild Wineries and Distilleries	2.0					
Franzia Bros. Winery			3.4	3.7	3.9	5.8
Gold Seal Vineyards, Inc.						2.6

502. Measuring the skewness of the market share distribution among the top four and top eight firms in the United States all wine market by the skewness of market share distribution among the top four and top eight United States wineries, the all wine market remained skewed during the period 1973 through 1976 (CX 366Y, Z–1).

503. Measuring the skewness of the market share distribution among the top four and top eight firms in the United States dessert wine market by the skewness of market share distribution among the top four and top eight California wineries, the dessert wine market remained skewed during the period 1973 through 1976 (CX 366Z–1).

504. Measuring the skewness of the market share distribution among the top four and top eight firms in the United States sparkling wine market by the skewness of market share distribution among the top four and top eight California wineries, the sparkling wine market remained skewed during the period 1973 through 1976 (CX 366Z–2).

D. Gallo and United Vintners Dominance

505. While United had a smaller market share than Gallo, United was still a dominant factor in the industry. This is reflected in the appraisal of the industry conducted for Heublein by the McKinsey study where, in its analysis of "Competitive Structure", it was stated, "Except For United Vintners And Gallo, Industry Is Composed Of Many Small Competitors" (See Finding 338, *supra*). This is confirmed by analysis of the industry.

506. In the all wine market in 1968, the second ranked competitor, United, shipped more than six times the wine gallonage of the third ranked competitor (CX 373D). In 1969 and 1970, the pattern was repeated with the second ranked competitor, now Heublein, shipping more than six times the annual wine gallonage of the third ranked competitor (CX 373F, H). In 1971, second ranked Heublein's annual wine gallonage shipments exceeded the third ranked competitor's shipments by a ratio of better than 4 1/2 to 1 (CX 373J). In 1972, second ranked Heublein continued to ship wine at a rate of nearly four to one in comparison to the third ranked competitor (CX 373K).

507. Subsequent to 1972, United, the second ranked domestic winery, continued to maintain a significant margin in wine shipments in comparison to the third ranked domestic winery in the all wine market. In 1973, United shipped 54 million gallons of wine in comparison to third place Almaden's 14 million gallons. In 1974, United shipped 49 million gallons in comparison to Almaden's 15 million gallons. In 1975, United's wine shipments jumped to 59 million gallons in comparison to Almaden's 16 million gallons, and in [108]1976, United shipped 56 million gallons in the all wine market in comparison to Almaden's 18.7 million gallons (CX 366Y).

508. United Vintners and Gallo are the dominant domestic producers of wine. In 1960, United produced 18.5 percent and Gallo produced 20.1 percent of all domestically produced wines entering distribution channels in the United States. By 1968, United accounted for 22.1 percent of all domestically produced wine entering distribution channels in the United States and Gallo accounted for 26.7 percent, totaling 48.8 percent of all domestically produced wine entering United States distribution channels (CX 330K). In 1976, United and Gallo combined produced 49.8 percent of all domestically produced wine entering United States distribution channels, accounting for 17.6 percent and 32.2 percent respectively (CX 381). From 1960 to 1976, United's and Gallo's combined share of all domestically produced wines entering United States distribution channels rose from 38.5 percent to 49.8 percent (CX 330K, 381).

509. In 1966, United produced 11.3 percent and Gallo produced 2.4 percent of all domestically produced sparkling wines entering distribution channels in the United States. (Data is not available for earlier years.) By 1968, United accounted for 12.8 percent and Gallo accounted for 13.6 percent, totaling 26.4 percent of all domestically produced sparkling wine entering United States distribution channels (CX 330M). In 1976, United produced 12.2 percent and Gallo produced 39.7 percent of all domestically produced sparkling wines

(CX 381). Between 1966 and 1976, the combined share of United and Gallo of all domestically produced sparkling wine entering distribution channels in the United States rose from 13.7 percent to 51.9 percent (CX 330M, 381).

510. Gallo and United are the dominant producers in the all wine market. The combined all wine market share of these two companies was 41.6 percent in 1967 and 41.9 percent in 1968. The combined all wine market share of Gallo and Heublein/United was 44.7 percent in 1969, 47.5 percent in 1970, 49.6 percent in 1971 and 46.7 percent in 1972 (CX 373B, D, F, H, J, K).

511. The combined dessert wine market share of Gallo and United was 43.0 percent in 1967 and 43.9 percent in 1968. The combined dessert wine market share of Gallo and Heublein/United was 44.1 percent in 1969, 44.5 percent in 1970, 45.7 percent in 1971 and 43.3 percent in 1972 (CX 373L, N, P, R, T, U).

512. The combined table wine market share of Gallo and United was 41.6 percent in 1967 and 39.2 percent in 1968. The combined table wine market share of Gallo and Heublein/United was 39.2 percent in 1969, 38.5 percent in 1970, 35.8 percent in 1971 and 32.9 percent in 1972 (CX 373V, Y, Z-2, Z-4, Z-6, Z-7; RX 15, 27). **[109]**

513. As explained above, I have excluded refreshment wines from the table wine submarket. Yet, volume-wise, refreshment wines constituted a substantial proportion of wine production, especially in the years 1970–1972. The following concentration ratios and universe figures for refreshment wines show that this segment of the all wine market was even more concentrated and skewed than any of the relevant submarkets; and that Gallo and United were the leading producers:

REFRESHMENT WINES
(% of market, 000 gals.)
(RX 15A–B, 27A–B)

	1967	*1968*	*1969*	*1970*	*1971*	*1972*
Gallo	56.2%	63.03%	58.30%	75.41%	82.39%	78.80%
	1563	3354	8321	22087	42562	50634
United	38.26	32.92	38.97	21.54	10.95	7.07
	1063	1752	5562	6310	5655	5440
Robinson-Lloyds	2.7	1.82	1.08	.36	.16	.30
	75	97	154	107	83	196
Monsieur Henri	.9	1.03	.77	1.50	2.35	3.30
	25	55	110	440	1212	2119

	1967	*1968*	*1969*	*1970*	*1971*	*1972*
Mogen David	.86	.48	.26	.14	2.22	6.10
	24		38	42	1148	3921
Monarch	.86	.6	.38	.63	1.65	3.51
	24	32	54	187	853	2255
Leonard Kreusch	.14	.07	.04	.04	.03	.03
	4	4	6	12	16	18
Gibson		.02	.16	.15	.08	.01
		1	23	45	41	9
Guild			.02	.19	.02	.11
			3	58	11	68
Seagram						.14
						88[110]

REFRESHMENT WINE
CONCENTRATION RATIOS
(derived from prior table)

	Universe (000 gals.)	*2 firm*	*4 firm*	*8 firm*
1967	2,778 gals.	94.46%	98.06%	99.92%[23]
1968	5,321 gals.	95.95%	98.80%	99.97%
1969	14,271 gals.	97.27%	99.12%	99.99%
1970	29,288 gals.	96.95%	99.08%	99.92%
1971	51,657 gals.	93.34%	97.91%	99.96%
1972	64,251 gals.	85.07%	95.48%	99.63%

Refreshment wine is not one of the submarkets involved in this matter, and Heublein was not engaged in this submarket at the time of the acquisition. Nevertheless, it is significant that when a new area for opportunity arose in the wine industry, the same two dominant companies, Gallo and United, were in a position to secure the lion's share and bring about an extremely concentrated submarket.

514. In 1967, Taylor Wine Co., Inc. ("Taylor") and United were the top two companies in the United States sparkling wine market,

[23] 1967 concentration ratio is for seven firms.

with a combined share of 24.6 percent. In 1968, Taylor and Gallo were the top ranked companies with a 24 percent combined share of the sparkling wine market; United ranked third with 10.7 percent of that market. Heublein/United and Gallo were the top two ranked companies in the United States sparkling wine market during the period 1969 through 1972. The combined sparkling wine market share of these two companies was 38.9 percent in 1969, 44.3 percent in 1970, 47.8 percent in 1971 and 47.6 percent in 1972 (CX 373Z–8 thru Z–13).

515. Gallo's great period of growth between 1970 and 1972 was connected in large measure with sharp gains in sales of its Boone's Farm line of refreshment wines. Since its peak in 1972, Boone's Farm has suffered erosion and Gallo has deemphasized refreshment wines. Gallo's emphasis in [111]advertising has shifted to Gallo's higher priced table wines and its Carlo Rossi brand of table wine (CX 366Z, Z–5, 367P).

516. As noted, Finding 489, *supra,* the record contains no individual company market share data subsequent to 1972. However, the record does show United increased its share in the all wine market in each of its calendar years 1973, 1974, 1975, 1976 and 1978. The record is silent as to 1977 (CX 361F, 543F).

E. Trend Towards Mergers and Acquisitions

517. The wine industry has been characterized by a significant trend towards mergers and acquisitions of wine suppliers from 1940 through 1977 (RX 485Q, 533A–D, 1216A–D; CX 209F, 299A–C; Tr. 4190, 5129–30, 6564, 6576, 8465–66, 9887).

F. Conclusions, Discussion of Impact of Merger and Case Law

Based upon the above findings of fact, I conclude that at the time of the acquisition the all wine market was concentrated and skewed, as were the table and dessert wine submarkets; and that the sparkling wine submarket was concentrated. Concentration ratios for the top two, four and eight firms in the market and submarkets in 1968 were:

	Top 2	*Top 4*	*Top 8*
all wine	41.6%	47.9%	57.4%
table wine	39.2	48.1	60.0

	Top 2	*Top 4*	*Top 8*
dessert wine	43.9	50.4	58.5
sparkling wine	24.0	41.9	62.7

In each of these markets, four-firm concentration exceeded the 40 percent threshold at which Professor Scherer deems industry interfirm coordination likely. In each of these markets, the eight-firm concentration substantially exceeded the 50 percent threshold at which Professors Kaysen and Turner characterize an industry as an oligopoly within which interfirm coordination and interdependence is likely.

Following the acquisition, the all wine market, as well as the table, dessert and sparkling wine submarkets remained concentrated. The two, four and eight firm concentration ratios in 1969 were:

	Top 2	*Top 4*	*Top 8*
all wine	44.7%	50.9%	60.3%
table wine	39.1	47.4	59.6
dessert wine	44.1	51.3	59.5
sparkling wine	38.9	54.9	71.9 [112]

The four and eight firm concentration ratios exceeded the Scherer and Kaysen and Turner thresholds discussed above. In addition, the four firm concentration ratios (except for table wine) exceeded the Kaysen and Turner thresholds for a tight oligopoly within which interfirm coordination and interdependence is deemed extremely likely.

The concentrated state of the wine industry is enhanced by its skewness. Skewness, as explained by economist Dr. Robert E. Smith (Tr. 5695), describes the disparity in size among the leading firms in an industry. As the preceding market share tables indicate, the all wine, table wine and dessert wine markets were skewed both in 1968 and in 1969, the year of the acquisition. The sparkling wine market appears to have become skewed in 1969. However, contrary to complaint counsel's assertion (CB, p. 20), I do not find that such skewness which occurred in that market in 1969 as a result of the merger is relevant to the issue of a possible or probable long-term increase in concentration in this submarket due to the merger. As previously noted (Finding 475 n. 21), in November 1969, the carbonation level of Lancers, which accounted for 99.7 percent of Heublein's 7.2 percent share of the sparkling wine market (derived

from CX 373Z–10, Z–11), was stabilized at a level below that at which it could be classified as a sparkling wine. In succeeding years, Complaint counsel include Lancers as a table wine. Thus, the increase in United's sparkling wine market share achieved by inclusion of Lancers was of consequence only from the date of acquisition, February 21, 1969, until November 1969. This transitory impact upon skewness is of no significance in this case which is concerned with long term probabilities.

Skewness is marked, however, in the other markets, and is important as an indication that the power accompanying strong market shares may be enhanced by disparate size in relation to other competitors in the market. The more skewed a given market is, the greater the likelihood that firms will be able to coordinate their activities effectively. The skewness of market structure is an independent determinant of the ability of competitors to coordinate their activities (Tr. 5696–97). In *Warner-Lambert Co.*, 87 F.T.C. 812 (1976), the Commission considered the issue of skewness of the market:

> In addition to conventional concentration ratios, the degree of asymmetry in size among leading firms is another factor which economists consider in assessing the competitive structure of markets. A given level of concentration measured by aggregate market shares held by top firms may portend different market conditions depending upon whether firms within the grouping are [113]relatively equal or quite disparate in size, with equality of size evidencing a more favorable climate for competition (at 870).

In *American General Insurance Co.*, 89 F.T.C. 557 (1977), the Commission also looked at skewness in the market and, while finding that skewness was not significant there, nevertheless held that: "An asymmetrical oligopoly may aggravate whatever lessening of competition may result from a merger. . ." (at 638). The disparity in size between United, the second leading firm, and the third leading firm in each market except sparkling wine is clear when expressed as the third ranked firm's percentage of United's volume:

PERCENTAGE OF THIRD RANKING FIRM'S SHIPMENTS TO THOSE OF UNITED

	1968	*1969*
all wine	17%	16%
table wine	36%	33%
dessert wine	15%	16.5%

(Source: market share tables, Findings 498, 499, 500, *supra*)

At the time of the acquisition, the all wine market, and the table wine and dessert wine submarkets were concentrated and skewed. In *United States* v. *Philadelphia National Bank*, 374 U.S. 321 (1963), the court held that " . . . if concentration is already great, the importance of preventing even slight increases in concentration and so preserving the possibility of eventual deconcentration is correspondingly great" (at 365 n. 42). HUV has raised arguments that the Court in *Philadelphia National Bank* rejected. HUV argues that Heublein's pre-acquisition market shares were insufficient to materially change the competitive structure of the industry. While Heublein's shares may have been small (see below, p. 114), the court in *Philadelphia National Bank* rejected such logic: "It is no answer that, among the three presently largest firms . . ., there will be no increase in concentration. If their argument were valid, then once a market had become unduly concentrated, further concentration would be legally privileged" (*Ibid.*).

The slight decline in United's share of the table wine market in the year of the acquisition does not vitiate a finding of high concentration in that submarket, nor prohibit a finding that the acquisition was illegal as to that submarket. In *RSR Corp.*, 88 F.T.C. 800 (1977), a case in which the second place producer with 12.16 percent of **[114]** production acquired the fifth place producer with 7.02 percent, thereby creating a new number two firm with 19.18 percent of industry shipments, the Commission noted that:

> . . . even were the record to point . . . to a decline in concentration exclusive of this merger, such a consideration would not weigh heavily in the face of the high absolute level of concentration and the increase therein caused by this merger. Evidence of a trend toward concentration may be relevant to show a violation in a case such as *United States* v. *Von's Grocery Co.*, 384 U.S. 270 (1966) involving comparatively small market shares and comparatively low concentration. It is obviously not necessary in a case involving large shares and high concentration (at 888 n. 18).

In 1968, Heublein's rankings and market shares were:[24]

all wine	16th	.79%
table wine	30th	.23%
dessert wine	13th	.54% (CX 373E, N, Z; RX 15, 27)

HUV argue that these increments to United's market shares resulting

[24] Sparkling wine is not being considered in light of the temporary nature of the increment. See p. 112, *supra*.

from the merger were so small as to be *de minimis* (RPF, pp. 190, 256, 263). The contention that such small increases cannot be considered in support of a finding that the acquisition had the proscribed anticompetitive effect, is without merit.

In *United States* v. *Aluminum Co. of America*, 377 U.S. 271 (1964), the Court found that an addition of 1.3 percent to the leading market share of 27.8 percent was anticompetitive in a highly concentrated market (two-firm concentration of 50 percent, four firm concentration of 76 percent) but one in which small independents still participated. The Court noted that the objective of the 1950 Amendments to Section 7 " . . . was prevent accretions of power which 'are individually so minute as to make it difficult to use the Sherman Act test against them' " (at 280).

In *Stanley Works* v. *FTC*, 469 F.2d 498 (2nd Cir. 1972), *cert. denied*, 412 U.S. 928 (1973), the court found that a market with a four-firm concentration ratio of 41 to 51 percent was "sufficiently concentrated to invoke the proscriptive sanction of the Clayton Act" (at 504), and held that " . . . the rationale underlying at least two Supreme Court decisions indicates that [the foreclosure of] Stanley's [115]1 percent is not a *de minimis* share of the . . . market" (at 506). Significantly, in responding to the dissenting opinion which noted that Stanley's market share was .47 percent smaller than the smallest foreclosure which had been held illegal prior to *Stanley*, the majority held that:

> In view of this market concentration . . . we cannot assume . . . that a difference of less than one-half of one percent—the difference between Blatz's 1.47 percent and Stanley's 1 percent market shares—is of decisive significance for a question of such controlling importance as whether one percent market control is, or is not, *de minimis* (at 507).

Adopting the Second Circuit's reasoning, in view of Heublein's entrenchment of United's market position (pp. 172–75, *infra*), the concentrated and skewed structure of the wine industry and Heublein's position as an actual potential expander (pp. 175–85, *infra*), Heublein's market shares at the time of the merger were not so insignificant that they should not be considered along with these various other factors.

HUV, relying primarily upon *United States* v. *Black and Decker Mfg. Co.*, 430 F.Supp. 729 (D. Md., 1976), assert that it is improper to

include in the same market wines *imported* and sold by Heublein and wines *manufactured* and sold by United. In that case, however, the court found no competitive overlap between the manufacturer and its retail seller. But, based on the facts of this case, considerable competitive overlap did exist between Heublein and United.

In *United States* v. *Continental Can Co.,* 378 U.S. 441 (1964), the Court held that "Where the area of effective competition cuts across industry lines, so must the relevant line of commerce . . . . " (at 457). Heublein and United compete at the distributor, supplier, and wholesale levels in distribution of their wine products, and both compete in promotion of their products at these levels and in advertising media to increase retail sales.

HUV have argued that Lancers Rose and Harveys Bristol Cream, the bulk of Heublein's gallonage, should not be included in its market share because they are imports and thus subject to supply volatility (in the case of Lancers) and the control of the actual owners (in the case of Harveys). To the contrary, the Lancers endeavor (jointly owned by Heublein) is a sophisticated, growing, and profitable business with no indication that supply problems are of any concern to Heublein. Neither is there any evidence of record that Allied Breweries, Ltd., owners of Harveys, participates in the marketing or distribution of [116]Harveys wines imported by Heublein for the United States market to the extent of usurping Heublein's control over such matters.[25]

HUV contend (RPF 240) that, as a general proposition, imports should be distinguished from domestic products in Section 7 cases, and rely on the following statement from W. Fugate, *Foreign Commerce and the Antitrust Laws,* 345, 351 (2nd ed. 1973):

> Imports are much more subject to being cut off, and they can be cut off merely by a decision of the foreign producer. Likewise, they can be cut off by tariffs and other governmental trade restraints.

HUV neglected, however, to include the immediately preceding sentence: "*Imports have been treated the same thus far,* although there is room for distinction" (emphasis added). The case law does not distinguish foreign from domestic products in computing market shares based on universe figures of total United States sales including imports. See, *e.g., United States* v. *Standard Oil Co. (New Jersey) and Potash Company of America,* 253 F.Supp. 196, 204 (D.N.J. 1966).

I also reject HUV's argument that the acquisition was procompeti-

[25] While the Harveys marketing plan is a joint effort of Heublein's brand manager, Harveys' representative and the advertising agency, the Heublein brand manager would make the final decision in the event of any disagreement (Tr. 4404).

tive. The contention is made that since Gallo has been firmly established as the leading producer in the wine industry since the mid-1960's (RRPF 13), " . . . the merger has aided—not hindered—compeition . . . " (RPF 250); and, that " . . . the 10.1 point increase in the eight-firm ratio between 1967 and 1972 was due to the increases of Gallo (9.5 points); Almaden (1.9 points); and Mogen David (1.5 points)" (RPF 251). While United's share did decline 4.2 points during this period, it remained the second leading firm far ahead of the third producer; its absolute volume increased impressively (from 38,226,600 gallons to 45,307,700 gallons); and in the six years since 1972, its market share has risen again in at least five of those years (Finding 516, *supra*).

HUV's contention that an otherwise unlawful acquisition is not anticompetitive if it results in the creation of a company better able to compete with a major competitor has been rejected as a matter of law. See, *e.g., Ford Motor Company* v. *United States,* 405 U.S. 562, 569–70 (1972); [117]*United States* v. *Bethlehem Steel Corp.,* 168 F.Supp. 576, 615–18 (S.D.N.Y. 1958); and, *United States* v. *Philadelphia National Bank,* 374 U.S. 321, 371 (1963).

At the time of the acquisition, the wine industry was a tight oligopoly and the market was skewed. While possessing a market share substantially smaller than that of the largest company, United had the second largest share which was several times larger than that of the company in third position. Heublein's acquisition of the second ranking producer immediately increased concentration by the extent of Heublein's share of the market. The acquisition also served to entrench United's dominant position and to remove Heublein as an actual potential expander (See pp. 172–85, *infra*). The effects of the merger, therefore, may be to substantially lessen competition.

VII. BARRIERS TO ENTRY OR EXPANSION IN THE WINE INDUSTRY

In order to further understand the overall impact of the acquisition upon competition in the relevant market and submarkets, we must proceed beyond the percentage increments added to United's market shares and the measurable percentages of additional competitive strength resulting from Heublein's elimination as an actual competitor of United. It is also necessary to examine what special competitive assets the Heublein organization brought to United, and whether United's second ranking position was entrenched by the Heublein acquisition in light of the characteristics of the wine industry.

Such analysis begins with an examination of whether there are high barriers to entry or expansion. Barriers to entry or expansion are conditions or arrangements which impede free entry into the relevant market on a level of sufficient magnitude to compete with industry leaders. Thus, the concept is better termed a "barrier to effective competition." *The Budd Co.,* 86 F.T.C. 569, 577 (1975).

Whether there are high barriers to entry is also relevant to the general question of whether the acquisition of a company may, for any other reason, have the effect of substantially lessening competition. For, if barriers are low any apparent anticompetitive effect could be dissipated in the long run by the entry of new competition. *Ekco Products Co.,* 65 F.T.C. 1163, 1207–08 (1964). Findings relating to barriers to entry or expansion in the wine industry on an effective competitive level follow.

A. Capital Requirements and Long Payout Period Barriers

518. The capital requirements to engage in wine production on a significant scale are great. Capital requirements for even a modest level of winery operation are substantial. Capital requirements to market wines in significant [118]volume, and establish brand recognition, are large. High capital requirements constitute a significant barrier to entry and expansion in the wine business (Tr. 5712–13, 5715, 5717).

519. Witnesses who addressed the subject of capital requirements noted the extremely high capital intensity of the wine business. The general manager of Souverain winery testified:

> It takes a lot of money to stay in the wine business. You can enter the wine business with one barrel and a tub to crush the grapes in, but if you want to go into a large national brand as we have chosen to do, it takes money to sustain your operation . . . It is definitely capital intensive . . . You don't enter in one year and make a profit the next year (Tr. 2139).

520. Dr. Richard Peterson, Winemaster and President of The Monterey Vineyard (Tr. 320), testified:

> I am sure everyone knows by now, the wineries' business is capital intensive in the extreme . . . (Tr. 359).

Dr. Peterson added that the winery business is "just like pouring money down a hole, you just keep putting money in before you can begin to sell wine to start with" (Tr. 359).

521. Patrick McDonald, a director of and consultant to Montcalm Vintners, Inc. (Tr. 5115), a failed new entrant testified:

> We elected to limit our capital involvement in the industry by not going into the

vineyard business or the grape business, but merely concentrating on the production of the wine and the marketing of the wine. Even limiting ourselves that way, we found out that for the type of operation that we wanted to become that it required what we considered to be an inordinate amount of capital (Tr. 5182).

522. Andrew Beckstoffer, the Heublein employee responsible for gathering and analyzing data with respect to the wine business, also judged the wine industry as capital intensive (Tr. 8979–80, 9026–28, 9074, 9085–86, 9092–93). [119]

523. Capital requirements to establish the plant and facilities for even a modest sized winery are substantial (Tr. 352–57, 674–75, 2107, 2119, 2142–44, 2245–50, 2154, 3452–53, 5136–38, 5181–82, 5184, 5188–89, 5218).

524. For example, the Souverain Winery, with capacity of approximately 2 1/2 million gallons, was built by the Pillsbury Co. in 1973 at a cost of $5,800,000 (RX 1192G; Tr. 2107, 2119, 2144).

525. Lee Chandler, the current general manager of Souverain considers Pillsbury's building costs of Souverain to have been "very low" relative to the average per gallon cost of building a winery (Tr. 2144). Mr. Chandler estimated that it would cost between $10 million and $11 million today to build the Souverain facility, not including the fountain and restaurant which are an integral part of the winery (Tr. 2142–43). He estimated that in 1973 or 1974, it cost between $3 and $4 per gallon of capacity to build a winery (Tr. 2144).

526. The relatively small size of the Souverain endeavor is apparent when we compare its 2 1/2 million gallon capacity with the 226 million gallon capacity of Gallo, the 95 million gallon capacity of United and the 57 million gallon capacity of Guild in 1976, and note that Guild was the fourth largest company in the all wine market in 1972 with but 3.8 percent (CX 373K, 458).

527. The cost of obtaining an adequate supply of grapes and bulk wine significantly contributes to the high capital requirements in the wine business, particularly for new entrants and expanding firms (Tr. 356, 3464, 3468–69, 5137, 5181–82, 5186–89, 5255, 8128–29, 8131; CX 413B).

528. In order to assure themselves an adequate supply of grapes, many vintners operate their own vineyards (Tr. 350, 352, 1008, 1953–54, 3202–03, 3453, 8972, 9005).

529. The costs of establishing a producing grape vineyard contribute to the high capital requirements in the wine production business by as much as $8,000 per acre (Tr. 360–62, 2237, 3453, 3466, 5181, 5184).

530. Since the production period of raw wine is seasonal, depending upon the seasonal maturation of grapes (CX 308U), wineries

must bear large bulk wine inventory costs from grape crush season to grape crush season (Tr. 2272; CX 240D, 247C).

531. The cost of maintaining inventories of bulk wine significantly contributes to the high capital requirements in the wine business, particularly for new entrants and expanding firms (Tr. 2140–41, 2235, 3464, 5181–82, 5184, 5186, 8131; CX 240D, 241D, 242C, 243C, 244D, 245D, 246D, 247C). [120]

532. Contributing to high capital requirements in the wine business for new entrants and expanding firms are the marketing costs of establishing brand recognition (Tr. 5184, 5188–89), as well as the costs of establishing and maintaining a winery sales force to solicit wholesale distributors and assist distributors' salesmen in obtaining and maintaining retail distribution of a winery's products (Tr. 630–31, 2122, 2125, 2174, 2222–23, 3324).

533. Also contributing to high capital requirements in the wine business is the extended payout period over which a winery must wait to begin to earn returns on its investment and recoup its full investment. This is a characteristic of the wine industry and constitutes a significant barrier to entry and expansion (Tr. 5712).

534. From the time of planting, it takes five to six years for a grape vineyard to produce a full crop (Tr. 361, 2238). In some grape growing areas, the length of time from planting to vineyard maturity may be as much as eight to nine years (Tr. 362).

535. The aging period required for wines, particularly red table wines, before they may be sold prolongs the period over which a winery must wait in order to earn income from its investment (Tr. 359, 1021–23, 2140–41, 5184, 5188–89). The time of grape crush to sale of the wine ranges from a minimum of six months to as long as ten years (Tr. 3133–34, 3161, 3223).

536. The length of time required to establish brand recognition also contributes to the long payout period during which a winery must wait to recoup its investments (Tr. 5713).

537. A substantial length of time is required before a new entrant in the wine industry becomes profitable. In the opinion of Dr. Peterson, Winemaster and President of The Monterey Vineyard in California, it takes six to ten years for a winery to become profitable from the initial time of building of the winery. If the new entrant plants its own vineyards, an additional four to eight years are expected to elapse before the winery becomes profitable (Tr. 363).

538. During the 3 1/2 to 4 1/2 years that the Souverain winery was owned by Pillsbury, Souverain did not make a profit (Tr. 2107, 2113). In 1976, Pillsbury sold Souverain at a loss (Tr. 2118–19). Since it was sold by Pillsbury, Souverain has operated at a loss and at less

than full capacity (Tr. 2141). The current general manager of the company expects it to be profitable within three or four years (Tr. 2144). [121]

539. California Growers Winery started its branded case goods business in 1971 (Tr. 1958–59). The President of California Growers testified on January 26, 1978: "I would say that during the last seven years that there has been virtually no contribution to profit on our proprietary case good business" (Tr. 1958–59).

540. Geyser Peak Winery in California was acquired by Joseph Schlitz Brewing Company in 1972 and began selling branded case goods in the fall of 1974 (Tr. 3452). In every year since 1974, Geyser Peak has sustained an operating loss (Tr. 3453–54; CX 389). Geyser Peak is not profitable today and is operating at less than full capacity (Tr. 3453, 3467). Geyser Peak's operating plan forecasts that it will be operating in the black within the next five years (Tr. 3467).

541. One notable example of substantial capital investment in the wine business is United's glass plant, valued at $18 million (Tr. 9221–22). The glass plant results in substantial cost savings to United (Tr. 9223).

B. The Distribution Barrier

1. Methods of Wine Distribution

542. Since the repeal of prohibition, 32 states and the District of Columbia have adopted licensing systems for distribution of alcoholic beverages. In general, these states have established three-tier systems of distribution. Ownership of each of the three levels of distribution—supply, wholesale and retail—must be separately maintained. Individual suppliers, wholesalers and retailers are licensed by the state to do business (CX 368 O). Generally, licensed suppliers may sell only to licensed wholesalers who, in turn, may sell only to other wholesalers and to retailers (CX 508A–B; state statutes cited under para. 2(c), p. 5, of Facts Submitted for Official Notice, dated May 2, 1978—noticed on record without objection; CX 368D, 511). These 32 states are referred to in the wine industry as "open" states (Tr. 4217).

543. The 18 remaining "monopoly" states, pursuant to the Twenty-first Amendment, exercise varying degrees of monopoly control over the wholesaling of alcoholic beverages (CX 368F). Eight states (Montana, Utah, Wyoming, Iowa, New Hampshire, Pennsylvania, West Virginia and Mississippi) monopolize the wholesaling of all wines and spirits (Tr. 9623–28). In 1969, these eight states accounted for 5.9 percent of total consumption of wines in the United

States, as measured by case shipments. In 1976, these eight states accounted for 6.3 percent of total wine consumption (RX 1231).

544. In four additional monopoly states (Idaho, Maine, Alabama and Michigan), the state monopolizes the wholesaling of spirits and wines over 16 percent alcohol by volume (Tr. 9623–28). [122]

545. The six remaining monopoly states (Oregon, Ohio, Washington, North Carolina, Vermont and Virginia) monopolize the wholesaling of spirits, but license others to wholesale wines (Tr. 9622–28, 9873–77).

546. The 18 monopoly states are often referred to as "control" states by wine industry members (Tr. 625, 4217).

547. It is more difficult to secure distribution in control states than in open states because control states' purchasing agents limit their purchases to those brands they select for sale at all outlets. In open states, while the seller may not be able to get full distribution, he still may be able to acquire some accounts (Tr. 4217).

548. As described by wine marketer and consultant, Stanford Wolf, the general methods of distribution for a California winery are as follows:

> A California winery can distribute directly to the consumer [in California]. Under our laws in California, he can distribute to wholesalers or combinations thereof. A winery distribution outside of California can be to wholesalers who are just wine wholesalers or to wholesalers which are beer and wine wholesalers, or to wholesalers that are spirits and wine wholesalers, or all three. There's distribution to the control state board in a limited number of states. These are the general methods of distribution (Tr. 7502).

549. A "primary" or "prime" distributor is a marketing and sales intermediary between the vintner and the wholesaler. A primary distributor usually handles a vintner's brand on a national or at least regional basis and acts on behalf of the brand owner in contacting and selling to wholesalers (Tr. 7503).

550. As a rule, the primary distributor purchases the products from the vintner and then resells to a wholesale distributor. The winery may then ship directly to the wholesale distributor or to primary distributor warehouses (Tr. 666).

551. Primary distributors frequently undertake marketing responsibilities, and have control over marketing and sales decisions (Tr. 2233, 2300, 2320, 2322).

552. A "broker" in the wine business handles the sale of a winery's products to the wholesaler without taking title and usually is paid on a commission basis. Brokers do not replace wholesale distributors in the distribution chain, [123]but serve as distribution intermediaries between the vintner and wholesaler (Tr. 7502).

553. Where permitted by state law, vintners sometimes organize their own direct wholesale operation. Such direct operations are generally unprofitable (Tr. 1033–34, 9718–21).

2. Importance of Effective Distributors

554. Obtaining good wholesale distribution is vital to the success of a wine company engaging in branded case goods sales (Tr. 1973, 2993, 3327).

555. Two factors were most frequently identified by witnesses to qualify a wholesale distributor as "good" or "effective". First, the wholesaler must have financial strength and be a good credit risk to the wine supplier. Second, the wholesaler must be capable of soliciting and servicing all the retail accounts within its market area (Tr. 644, 662–63, 1970, 1994, 2123–24, 2994, 4208–10, 4699, 4701, 4703, 6853).

556. Part of a wholesaler's ability to cover retail accounts adequately is determined by the size of its sales force. In addition, the sales force of a "good" or "effective" distributor must be trained to sell wine (Tr. 644, 1972, 2123, 4208–09). Aside from the ability of a wholesaler to be a "good" distributor, it tends to be "good" for a winery which is a significant supplier to it (Tr. 1972, 1994).

557. A significant mark of a "good" or "effective" distributor is the wholesaler's strength with the retail trade in securing shelf space for the products it distributes (Tr. 6853). One vintner explained how a good distributor helps get shelf facing. He is already selling the retailer one of the must items in his store. Each of the distillers has one or two or three must items. There may be 20 or 30 items without which no retail store could live (Tr. 655).

558. A weak distribution system impedes the ability of a new winery entrant to generate sufficient volume of sales to spread fixed operating costs. The larger the size of the new entrant, the more important it becomes to secure effective wholesale distributors (Tr. 2111, 2121, 2141, 2176, 5181–82, 5185).

559. Although not all large wine and spirits wholesale distributors may be said to be "effective" wine distributors (Tr. 3022), it is generally true that the large wine and spirits wholesalers tend to have the requisites to handle wine effectively for a significant new entrant or expanding firm (Tr. 641–42, 662–65, 1057–58, 1063, 1240–41, 2123–24). [124]

560. Strong selling spirits lines give wine and spirits wholesalers strength with the retail trade (Tr. 650–51, 662–65, 1085; CX 115B).

561. There are few wine only wholesalers (Tr. 663, 1081–82, 4210). It is very difficult to support a wholesale organization on the volume

generated by selling wine alone (Tr. 3311–12, 4210). With the exception of the Gallo and United direct wholesale operations, wine only wholesalers tend to be weak (Tr. 663–65, 5169, 5185, 5230).

562. Except in those states where the state reserves to itself the wholesaling of spirits, beer distributors which also distribute wine tend to be less effective wholesalers of wine than wine and spirits distributors (Tr. 661, 5147–48, 5153, 6669).

563. If a substantial volume of wine were sought to be wholesaled by a wholesaling facility whose major business is beer, the beer and wine would be incompatible products within that facility because of their different methods of sale and delivery (Tr. 661–62, 686, 3351, 3354, 3364, 3371, 3420, 3610, 6836).

564. It is not surprising, therefore, that wine suppliers generally prefer to distribute their wines through wholesalers who carry both wine and spirits (Tr. 626, 662–63, 1083–84, 1240–41).

565. Few wholesalers whose major business is distributing beer also distribute wine (Tr. 2999–3000, 3428; CX 218A thru Z–316).

566. The current president of the California Beer Wholesalers Association could name only one California beer wholesaler, other than his own company, which distributed only wine and beer (Tr. 6221, 6245, 6284–86).

567. Guild, Canandaigua, California Wine Association, Paul Masson and Christian Brothers are distributed primarily through wine and spirits wholesalers, except in those states where the wholesaling of spirits is undertaken by the state and wine passes through wine only or beer/wine wholesalers (Tr. 3000, 4210–12, 4689–90).

568. Asked to name United's wine wholesalers who were beer distributors, Mr. Powers, the Chairman of the Board of United, named only one beer distributor in the entire United States who was not either located in a monopoly state where independent spirits wholesaling is prohibited or was not also a distributor of spirits (Tr. 9638–39, 9873–77). [125]

569. United's wines are wholesaled in the top 20 metropolitan markets for the sale of wine (Tr. 9872). United, however, has neither a beer/wine only wholesale distributor nor a wine only distributor, with the exception of those areas where United has its own direct all-wine wholesale operation, in any of these markets (Tr. 9812–16). This clearly demonstrates the importance of being able to utilize combined wine and spirits wholesalers.

3. Important Areas of Distribution

570. From 1962 through 1976, California, New York, Illinois, New

Jersey, Pennsylvania, Michigan, Florida, Ohio, Texas and Massachusetts have consistently been the top ten states in terms of consumption of wine (CX 297G; RX 1231). These ten states collectively received 70.4 percent in 1962, 69.2 percent in 1968 and 65.6 percent in 1976 of all commercially produced wine entering distribution channels in the United States (CX 297G).

571. Wine consumption is concentrated in the major metropolitan population centers where regular users of wine are also concentrated (CX 379U, 386B; Tr. 7524, 8353–54, 9619).

572. For the introduction of new brands of wine, wine marketers tend to focus upon the major metropolitan markets where wine consumption generally is concentrated (Tr. 1965; CX 3520).

4. Limited and Declining Number of Effective Distributors

573. New entrants aspiring to significant size and independently owned wineries find it difficult to obtain effective wholesale distributors. The number of effective wine wholesalers is limited (Tr. 655, 681, 1057–58, 1063, 1969, 1984, 2111, 2121, 5154–55, 5185, 5188–89).

574. Montcalm Vintners, Inc., attempted to acquire other wine companies in order to get distribution by virtue of the other companies' associations with wholesalers (Tr. 5143, 5194–95).

575. For at least the past ten years, the departure from business of wine and spirits wholesale distributors and the mergers and consolidations of wholesalers have reduced the number of independently owned wine and spirits wholesalers (Tr. 643–46, 652, 680, 1058, 1064–65, 1093, 2996, 3525–27, 7182–85, 7228, 7236, 7289–90, 7306, 7568, 6813, 6827, 6831, 6875, 7370–71).

576. Overall, there are fewer wine and spirits wholesale distributors than there were ten years ago (Tr. 643, 6831), and fewer "good" or "effective" distributors (Tr. 1057–58, 2996). [126]

577. The number of large distributors in metropolitan markets, with populations over one million people, has also been declining (Tr. 1057–58, 4209–10).

578. On the average, there are four to six large wholesale distributorships for a given major metropolitan market (Tr. 641–42, 3019, 3021). For example, within the Los Angeles area, there are five major ownerships (totaling nine distribution branches) of wine and spirits distributors (Tr. 6946, 6951). In the New York metropolitan area, there are five major wine and spirits wholesalers, each having separate divisions (Tr. 7250; CX 395Z–12).

579. In Washington, D.C., where per capita consumption of wine is the highest in the nation, there are roughly a dozen wholesalers who handle wine (Tr. 7572; CX 379S).

580. Illustrative of the substantial difficulty which wineries, particularly new entrants aspiring to significant size, have in endeavoring to find effective distributors in major metropolitan markets is the experience of California Growers Winery. Mandia is California Growers' current wholesale distributor in New York City, but it is not a major distributor. Mandia covers less than 1 percent of the New York metropolitan area in its endeavors to sell California Growers' wines (Tr. 1984).

581. In both 1970 and 1976, New York was the second largest metropolitan area in the United States for case sales of wine, behind the Los Angeles-Long Beach metropolitan area (CX 379U, 386B).

582. Even California Wine Association ("CWA"), a reasonably well-established, independently owned wine supplier, has experienced significant difficulty in securing a New York City wholesale distributor for its wines. CWA has not been able to secure a meaningful distributor in New York since CWA's previous wholesaler in New York closed its doors in 1977. CWA did have a wholesale distributor, a small house called Testa, in metropolitan New York. Testa had no salesmen and buys about 500 cases from CWA every three or four months (Tr. 1008, 1059, 1105).

583. One central cause of the declining number of wine and spirits distributors is the low profitability of liquor wholesaling. Generally, the wholesale business operates on a very small net profit ranging from 1 percent to 1 1/2 percent to 2 percent before taxes (Tr. 3536).

584. The president of one large wholesaler, whose sales were about $78 million in 1977, testified that the cost of operations in the wine and spirits wholesale business has increased rapidly, more rapidly than profits (Tr. 7356, 7390). Mr. Hermann, President of McKesson Wine and Spirits Co., testified: "Liquor wholesaling trends are for a high volume, low margin industry" (Tr. 7233). McKesson consolidated [127]wholesaling facilities in response to pressures squeezing the industry's profit margin (Tr. 7289–90, 7306).

585. Demonstrating the decreasing number of substantial wholesalers is the decrease in membership of the Wine & Spirits Wholesalers of America, Inc. ("WSWA"), a trade association of major wine and spirits wholesalers in the United States (Tr. 3507–08, 3511, 3517–18).

586. There are no other trade associations for the wholesale liquor industry on a national level comparable to WSWA (Tr. 3512). The WSWA convention is the largest convention of the industry (Tr. 8670).

587. The General Counsel of WSWA believed that it had the vast

majority of substantial wholesalers operating in the United States (Tr. 3541); that there are relatively few substantial wholesalers who are not members of WSWA (Tr. 3511). By "substantial wholesalers" he meant "those people that have capital invested or substantial capital invested in it and are in a position to service suppliers adequately" (Tr. 3717–18).

588. Excluding monopoly states, WSWA had 435 members plus 281 branches of members in 1973, 428 members plus 276 branches of members in 1974, 427 members plus 257 branches of members in 1975, 399 members plus 229 branches of members in 1976 and 383 members plus 227 branches of members in 1977 (Tr. 3543–44).

589. In monopoly states, WSWA had 29 members and three branches in 1973. In 1977, there were 37 members and three branches of members of WSWA in the monopoly states of Maine, Michigan, Ohio, Oregon and Virginia (Tr. 3544).

5. Supplier Influence

590. As Dr. Richard Peterson, President and Winemaster of the Monterey Vineyard, testified:

[P]ower, the muscle, whatever it is called, leverage, I think that it is common in the wine industry. I don't like it, but I think it is there (Tr. 489).

591. Dr. Peterson explained wine supplier "leverage" to mean:

Well, someone has muscle or someone has leverage with someone else, I guess I will say A has muscle with B when B needs A to do something or to continue doing what he is doing. If it is a distributor, the distributor [128]might be carrying a wine line that he continues to want to carry, maybe it is growing or doing quite well. That distributor will bend over backwards to continue that wine line if possible (Tr. 378).

592. In the judgment of Fred Switzer, General Counsel of WSWA, a major liquor supplier theoretically could influence one of its wholesalers not to take on a particular line or product of competing suppliers if the major supplier had the "leverage to influence the wholesaler" (Tr. 3551–52).

593. In Mr. Switzer's view, "Heublein would have the normal leverage that would be associated with the importance of their brand in a wholesaler's house" (Tr. 3580; see also Tr. 3612, 3614, 3628–30). Mr. Switzer observed that "Heublein is considered an important factor in the market [by wholesalers]" (Tr. 3614).

594. Heublein's General Counsel, George Caspar, acknowledged the existence of spirits supplier leverage in a transmittal to the Federal Trade Commission during the formal investigation of the merger. Mr. Caspar stated:

A number of the questions has indicated a concern on the part of the Commission's staff as to the possibility of foreclosing distribution by the entry of liquor companies into the wine industry. This is obviously a legitimate concern . . . Certain distillers . . . can, and often do, dominate and control their distributors (CX 327Z–13 through Z–14).

595. Robert Ivie, President of Guild Wineries & Distillers, defined a "captive house" as a wholesaler in which a particular supplier is in a strong enough position to heavily influence the wholesaler's activities (Tr. 3001).

596. A supplier's influence over the wholesaler's activities could affect the ability of other companies to obtain distribution through that wholesaler. Guild has experienced problems in obtaining distribution with a captive house (Tr. 3001–02).

597. The importance of a major spirits supplier to a wholesaler and retailer has been described by the President of Wine World, a producer and marketer of wines:

Any time you have a successful liquor brand such as Smirnoff [Heublein's major brand] or [129]Canadian Club or Cutty Sark Scotch, any distributor would have to have some interest in that. If he was in the liquor business or had thoughts of going into the liquor business, it is just common, good business practice to check the interest in a brand such as that (Tr. 3336–37).

598. The major spirits suppliers have considerable power to influence the operations and decisions of wine and spirits wholesalers (Tr. 641, 1064–65). Whenever a distiller acquires a winery, it makes it more difficult for an independent to compete for distribution (Tr. 1057–60).

599. Joseph E. Seagram & Sons, Inc., Heublein, Inc., National Distillers & Chemical Corp., Schenley Industries, Inc., Fleischmann Distilling Corporation, Hiram-Walker-Gooderham & Worts, Ltd. and Brown-Forman Distillers Corporation are the distilled spirits suppliers most frequently identified in the record as major suppliers (Tr. 640–41, 656, 1065, 3361, 3532, 6543–44, 6773, 6947, 7210, 7312, 7359).

600. Each of these spirits suppliers owns and operates one or more domestic wine companies and/or one or more wine importing companies (CX 373K; Tr. 8692–93). For example, Joseph E. Seagram & Sons, Inc. owns and operates Paul Masson Vineyards, Inc.; and National Distillers & Chemical Corporation owns and operates Almaden Vineyards (CX 373K).

601. It is a common practice in the wine industry that a wine supplier obtaining a new product or group of products—whether by new product development, by acquisition, or by virtue of a primary distribution arrangement with a wine producer—endeavors to place the new product(s) in wholesale distribution houses with which the

supplier has an ongoing relationship (Tr. 627, 636–37, 646–47, 2137, 2232, 3310–11, 3360–61, 3379–82, 3405, 3438, 3837–38, 3866, 3925–26, 3985–86, 4288–89, 4689, 4693, 5165–66, 5194–95, 5237, 7226, 7298, 7312, 7359, 7531–32, 7582–87, 7952–53, 8483–84, 9644; CX 325, 218Z–9, 256Z–34, 533A–B).

602. When Heublein obtained the agency for importing and marketing Harveys ports and sherries in 1957, it placed the Harveys products in the wholesalers in which the Heublein spirits products were already being carried. This was in addition to retaining the distributors through which the Harveys wines were already being sold (Tr. 3985–86).

603. When Heublein purchased Vintage Wines, Inc. in 1965 and obtained the Lancers trademark, Heublein retained the existing distributors for Lancers wines and added additional [130]ones. The majority of the additional distributors were already carrying Heublein alcoholic beverage products (Tr. 4288–89).

604. When United introduced the Inglenook Navalle brand of wines, in most cases, the wholesale distributors used for the distribution of Inglenook were United's preexisting Italian Swiss Colony distributors (Tr. 7952–53).

605. United's Fiscal 1972 Profit Plan and Major Programs established a "sales plan" to "Place Annie Green Springs in Petri (a United brand) houses if product is rolled out nationally" (CX 256Z–34).

606. As specifically evidenced for the period July 1972 to January 1975, United's rule of thumb in test marketing and introducing new products was to place them with wholesale distributors which were already handling United's Italian Swiss Colony line. In order to expand the geographic distribution of Inglenook products, United generally went with the same wholesalers that were handling United's other wine lines (Tr. 3310–11).

607. Heublein chose 11 introductory markets for the distribution of Beaulieu brandy. In July 1970, in nine of those markets, the distributors targeted by Heublein were existing distributors of Heublein products. Heublein targeted an existing distributor of Beaulieu wine in one of the remaining two markets and in the other utilized a broker (CX 93M, 94B, 324, 325, 356Z–5, Z–37).

608. Effective January 1, 1977, Julius Wile Sons & Co., Inc., became the sole marketing agent for the wine products of Souverain Cellars (Tr. 2126). Julius Wile is a subsidiary of Standard Brands, Inc. (CX 299B) and markets imported liquers and wines (RX 518C; Tr. 2125). Julius Wile placed Souverain in wholesale houses that had handled other Julius Wile products for many years (Tr. 2137).

609. As Fred M. Switzer, Executive Vice President and General Counsel of the Wine & Spirits Wholesalers of America ("WSWA"), testified, generally the alcoholic beverage supplier "expects the wholesaler to assist him in connection with his whole family of lines" unless the supplier has split his lines between different distributors in the same market. "But if he has only one distributor in the area he naturally expects him to handle the entire line" (Tr. 3550).

610. One factor motivating liquor wholesalers to handle the full family of products of an alcoholic beverage supplier, including its wines, is the desire of the wholesaler to maintain or secure an exclusive relationship with the supplier for one or more products of the supplier. One Washington, D.C. [131]wholesaler who distributes United's products explained, "We don't want him dealing with anybody else" (Tr. 6412). In the District of Columbia area, liquor wholesalers generally handle product lines on an exclusive basis (Tr. 6402).

611. Wholesalers prefer to obtain long-term exclusive distribution rights, or primary marketing area rights, to a wine or spirits brand or line, in contrast to sharing primary distribution rights with another wholesaler (Tr. 6412, 6841–44, 7383–89). To the extent a wholesaler is successful in building sales of an exclusively distributed brand within his marketing area, that wholesaler alone enjoys the repeat wholesale sales of the brand (Tr. 3366–67, 6843, 7385).

612. Normally, a wine and spirits wholesaler has no control over whether or not he obtains a brand or line of wine or spirits on an exclusive basis (Tr. 6844).

613. Wholesalers of wines and spirits generally do not have written contracts with their suppliers (Tr. 3385, 6787, 7352, 7403). And when a liquor supplier does have a contract with a liquor wholesaler, it is universally true that the supplier writes the contract (Tr. 3533).

614. Although WSWA has recommended to wine and spirits suppliers that they write contracts which provide for termination of the right to distribute the supplier's brands only for good cause, generally those recommendations have not been adopted by suppliers (Tr. 3533–34, 3545–46, 3565).

615. Wholesalers of wine and spirits want to maintain good relations with their suppliers. To that end, they may purchase and carry a supplier's slow moving products and so lose money (Tr. 3551). When a wholesaler takes on an additional product which he deems to be a strong seller, he also takes on additional weaker selling items of the line in order to obtain the stronger selling product (Tr. 3393–94).

616. Heublein's own agency relationship with Harveys exempli-

fies the obligation imposed by a major supplier. The obligation was articulated by Heublein's Executive Vice President:

Q. Was it Heublein's desire to take on Harvey's Selections?
A. No, it was not. It was Harvey's desire to sell some imported wines in the United States.
Q. Then why did you take them on?
A. Because we were asked to and we did have the Harvey's Bristol Cream and sherries and ports, and [132]we felt it somewhat of an obligation, so we said, "Yes, we will take it on" (Tr. 4414).

617. Vintners consider the offering of a broad line of wine products to be an attractive selling point to wholesalers since the vintner can supply all the wholesalers' needs (Tr. 1100, 1980, 2024). When this is done, it makes it more difficult for other wine companies to compete for wholesale distribution (Tr. 1100).

618. When wholesalers carry full lines of their major or desired suppliers, this makes it all the more difficult for a new winery which is starting with a limited line to supplant a type of wine the wholesaler already carries.

619. A wholesaler is reluctant to take on an additional substantial line of wines which includes products of the same types and price points as lines of wines he is already carrying. However, a weak or small line of wines may not meet the same objection and unique individual items of wines may also readily find distribution (Tr. 507, 640–41, 1969, 1973, 2994, 3366, 3402, 3406, 4206, 5159–60, 6799, 6960, 7588).

620. Alcoholic beverage supplier influence with a wholesaler is a function of the number and kinds of product offerings of the supplier and the dollar volume of business to be produced by the supplier's products. The larger the number and kinds of products of the supplier and the dollar volume of business represented by the supplier's products, the greater the influence of the supplier with a wholesaler (Tr. 1042, 1064–65, 1068–69, 1089, 1100, 4799–4801, 5004; CX 395Z–11 thru Z–13).

621. The power of an alcoholic beverage supplier to terminate its wholesalers without cause is a source of influence of the supplier over the wholesaler. Mr. Switzer, General Counsel of WSWA, explained that, although major liquor suppliers seldom terminate their wholesalers, "the power to terminate arbitrarily without cause gives the supplier an influence, a leverage over the daily day-to-day operations of the wholesaler in the way he runs his business and it deprives him of a certain independence" (Tr. 3547); Mr. Switzer also stated, "Where a supplier whose brands represent a substantial portion of the wholesaler or distributor's business terminates the

franchise, it is a serious business setback to the wholesaler, depending upon . . . " the circumstances, " . . . but in the majority of the cases it is a very serious setback" (Tr. 646, 3536).

622. Prompted by its inability to get wine and spirits suppliers to add provisions to their contracts with wholesalers which provide for good cause termination only, WSWA [133]has recommended the adoption of state franchise security laws to that effect (CX 554, 555A–C; Tr. 3565, 6838, 7400–01).

623. WSWA is interested in state franchise security laws to protect wine and spirits wholesalers not only against unjust terminations but also against the possibility that the supplier exercise a threat of termination implicitly or explicitly to influence daily operations of the wholesaler to his detriment (Tr. 3561).

624. Franchise protection laws, including the subject of "leverage" of suppliers over wholesalers in the sale of spirits has been on the agenda and has been discussed at WSWA conventions.

625. Major spirits lines frequently are a substantial source of revenue to large wine and spirits wholesalers (Tr. 3352, 3362, 6551–52, 6612, 6658–59, 6812, 6855, 6947–48, 7356–58). They may well be essential to the very existence of the wholesaler (Tr. 646–47, 1064, 1070–71, 1082–83).

626. Major spirits suppliers frequently have primary or exclusive distribution arrangements for a product line or lines with distributors in a metropolitan market (Tr. 640–42, 656, 4689, 4693, 4695, 4697, 4708–09, 6402, 7357, 7388–90). A spirits supplier may give an exclusive on one product or group of products to one wholesaler and an exclusive on other products to another wholesaler for a given territory (CX 218Z–12 thru Z–33).

627. The products of the major spirits suppliers tend to be distributed by the principal wine and spirits wholesalers in a given metropolitan market (Tr. 640–42).

628. The commitment of a wholesaler to handle the newly acquired wine products of an established supplier may itself have an exclusionary effect upon competing wine suppliers (Tr. 1068–69).

629. To the extent that offering a wholesaler a broad line of spirits and wines influences the distributor to accept the wine line, suppliers of more limited wine product offerings are disadvantaged in obtaining and retaining effective wholesale distribution (CX 395Z–11, Z–12; Tr. 1064–65).

630. Vintner Weibel testified that when he sought new distributors in 1968, "I would automatically have crossed off all Seagrams distributors because Seagrams is automatically Paul Masson. I was

barred from them. You have National Distillers with Almaden in a similar situation" (Tr. 639–40).

631. Bruno Solari, President of United prior to its acquisition by Heublein (Tr. 4686), was concerned that the entry of liquor suppliers into the wine business would cause [134]United to have to rely upon less effective distributors (Tr. 4686, 4696–97, 4699–4701, 4703; CX 295Z–11 thru Z–13).

632. Mr. Solari's explanation of why it was necessary for United to set up a direct wholesale operation in Southern California, exemplifies supplier influence:

I had one [wholesaler] in Southern California, Bohemian Distributing Company, but they tied up very closely with Seagrams. When that happened, we had to step out and start our own thing in Southern California (Tr. 4708–09).

633. Stuart Watson, Chairman of the Board of Heublein, related Mr. Solari's concerns of the effect of National Distillers' Almaden acquisition and his expectation of the beneficial effects of the merger of Heublein and United:

He [Solari] was concerned that now that National Distillers owned Almaden that the future of United Vintners and those distributorships would be in jeopardy and that it was important in looking ahead for United Vintners to affiliate itself with a company like Heublein who had access to these distributors because it was a principal alcoholic beverage company distributed through the same channels (Tr. 4967).

634. Mr. Watson also testified:

Many of the Italian Swiss Colony distributors across the country were National [Distillers] distributors because of this heritage and so there was concern on the part of the management of United Vintners from a marketing standpoint about the relationship of the distributors. There was a duplication, in other words (Tr. 4962).

635. Indeed, just five days after the merger, Heublein's Senior Vice President for the Smirnoff Beverage and Import Company reported to Mr. Watson as follows:

Knowles [Beaulieu's Vice President] also told me that Pete Jurgens of Almaden Vineyards [owned by National Distillers] is very much concerned over the fact that U.V. is in so [135]many National Distiller's wholesalers. Almaden's West Coast sales manager has asked the salesmen to list specific instances where the promotion and sale of Inglenook may be impeding the progress of Almaden (CX 208B).

636. Fred Weibel, President of Weibel Champagne Vineyards since the 1950's, explained supplier influence:

Q. What has been your experience in remaining in a wholesale liquor house where in that house there is present a liquor company which also owns a wine company?
A. You are there by the grace of the liquor company until they blow the whistle on you (Tr. 648).

637. Wine and spirits wholesalers desire to maintain good relations with their major suppliers (Tr. 3557) and decline to carry wine or brandy products of certain vintners for fear of jeopardizing their relationships with their major suppliers (Tr. 640–41, 1070–71, 3557).

638. Wholesalers have declined to purchase The Monterey Vineyard's wines due to leverage exercised by wine suppliers of the wholesalers. In one instance, it appears that Paul Masson exercised leverage and in another either United's or Almaden's influence precluded the purchase of Monterey Vineyard wines (Tr. 381–82, 393–94).

639. A limited number of wine items of a new wine supplier may achieve distribution. However, a broad line of wine items of a wine supplier can pose a threat to other wine suppliers at the wholesale distribution level and may encounter major supplier influence (Tr. 385, 698).

640. Dr. Peterson, when seeking wholesale distribution for the wines of The Monterey Vineyard, a new entrant, found it very difficult to get distribution in wholesale houses whose major suppliers were Heublein, Seagram, Schenley, National Distillers or Hiram Walker. However, after Monterey Vineyard's failure and reorganization as a smaller producer, Dr. Peterson found it easier to get wholesale distribution (Tr. 354, 384–85).

641. Christopher Carriuolo, then Senior Vice President of Heublein's Smirnoff Beverage and Import Company (CX 357Z–5), when discussing the possibility of a primary distribution arrangement between Heublein and Beaulieu Vineyards, reported to Mr. Watson in February 1969 that: [136]

[He] . . . pointed out [to the national sales manager of Beaulieu] that such an alliance would be an advantage to BV in guaranteeing good distribution, merchandising coverage, development of wine lists, technical know-how, distribution and warehousing facilities, etc." (CX 208B).

This representation had been made because of Beaulieu's inability to expand beyond the few markets the product was then being sold in (Tr. 8787).

642. In documents prepared by Heublein and presented to the Allied Board of Directors as well as at Allied member meetings, Heublein represented that one of the advantages to accrue to United from the merger would be "marketing strength through wider distribution" (CX 341, 342). This meant that, having access to Heublein's distributors, United would be given greater marketing strength (Tr. 2467, 2487).

643. Heublein represented that since Heublein's and United's products were compatible, United's wine distribution could be enhanced by Heublein's distributor organization. Smirnoff vodka was cited as a product which could be used to secure better distribution for United's wines; and it was stated that by having Lancers and Smirnoff together with United's wines, distribution for both companies could be increased (see Finding 258, *supra*).

644. Heublein's influence at the wholesale level is recognized by wine suppliers (Tr. 640–41, 650–51, 3336–37, 4226). As the President of Weibel Champagne Vineyards testified:

Q. Now, do you have an opinion as to Heublein's potential to exercise influence as to exclude your company from wholesale distributors?

* * * * * * *

A. They certainly have the power if they were to elect to exercise it.
Q. Why do you say that?
A. Heublein is extremely important to that distributor. Obviously he is making a lot of money off the Heublein line (Tr. 650–51). [137]

645. A Heublein internal management communication reveals Heublein's awareness of the leverage it had at both the wholesale and retail levels. George McCarthy, Brand Manager of Lancers, wrote to Walter Cohan, Vice President of Marketing of Heublein:

The opportunity for Vinya in many ways relys [*sic*] on the continued growth of Lancers. We are able to insist on Vinya distribution and display mainly because of the Lancers leverage we have in many distributors. At the retail store level, the Lancers leverage also allows us Vinya distribution and display. Any serious softening of this leverage can result in a loss of Vinya potential as well as Lancers.

Lancers as a high volume, high profit item, also allows us distributor and promotion leverage for new product introductions. Since Lancers is in many distributing houses that are not Smirnoff houses the importance of this brand gives us additional alternatives (to main line distributors) for distributing new products. Since Lancers as a wine product is not under the same restrictions as liquor, it also gives us promotional opportunities for new products. Obviously this leverage is only effective if Lancers continues to be a high volume growth item with strong consumer demand (CX 115B; see also CX 114 for identification of personnel).

This document details the leverage enjoyed by reason of Lancers in addition to that in houses that carry Smirnoff, where leverage is assumed.

646. Heublein's Vinya Marketing Plan for fiscal 1972/73 stated:

[W]e will insist on all Lancers distributors stocking and distributing this product. As a general rule, we have already notified sales personnel that all Lancers distributors should carry a minimum of 10% of their Lancers inventory in Vinya (CX 352P). [138]

647. In 1976, of the top 25 United States metropolitan areas for

consumption of wine, measured by case sales, 19 were also among the top 25 metropolitan areas for the consumption of vodka, measured by case sales (CX 313C, 379U).

648. In 1976, of the top 50 United States metropolitan areas for consumption of wine, measured by case sales, 41 were also among the top 50 metropolitan areas for the consumption of vodka, measured by case sales (CX 313C, 379U).

649. In 1976, of the top ten state markets for wine consumption, measured by case sales, eight were among the top ten state markets for vodka consumption, measured by case sales (CX 379S, 383E).

650. In 1976, of the top ten state markets for wine consumption, measured by case sales, seven were among the top ten state markets for tequila consumption, measured by case sales (CX 379S, 383H).

At the time of the merger, Heublein ranked first in the United States in the sale of vodka (Finding 16, *supra*). Its Smirnoff brand was not only the world's largest selling vodka, but was the second best selling brand of liquor internationally. It was the third best selling distilled spirits brand in the United States and was gaining on second place (Findings 29, 30, *supra*). Lancers was the best selling imported wine in the United States (Finding 38, *supra*). Heublein's tequilas accounted for more than 50 percent of the United States tequila market (Finding 39, *supra*). In addition, Harveys Bristol Cream was a "call item" (Finding 35, *supra*).

651. Considering Heublein's strength in the very markets where the sale of wine is concentrated, Heublein's potential leverage and influence on wholesalers to carry United's products is all the greater.

652. Due to possible repercussions with respect to this administrative proceeding, a Heublein executive, Christopher Carriuolo, who was then the Group Vice President of the Beverages Group of Heublein which included supervision of United (CX 357Z-5; Tr. 4316), instructed Mr. Richard Maher, Jr., United's Vice President of Sales and Marketing, not to seek to combine Heublein distributorships with United distributorships. Mr. Maher testified as follows:

Q. Now, sir, for the period of time that you were employed by United Vintners, were you under instructions from any Heublein employees not to seek to combine the wholesaling efforts of United Vintners with the wholesaling of Heublein products? [139]

* * * * * * *

A. Yes.

By Mr. Masson:

Q. What were those instructions?

A. The general discussion was that we *should not go ahead and seek to combine*

Heublein distributorships with United Vintners distributorships. However, there was no limitation upon individual cases.

Q. Who gave you those instructions?

A. I believe it took place in a conversation with Mr. Carriuolo and Mr. Oster. I believe he was there.

Q. And who is Mr. Carriuolo?

A. At that time, he was group vice-president of the spirits and wine division, whatever the exact title was.

Q. Were any reasons articulated to you by Mr. Carriuolo why you should not seek to combine the wholesaling efforts of United Vintners with Heublein?

A. Complications relative to the FTC case.

Q. This FTC case?

A. Yes. (Emphasis added; Tr. 3317–19)

This testimony evidences Heublein's understanding of the distribution advantages afforded by the merger and its intention to utilize those advantages. It also refutes the evidence upon which HUV rely (RR 252), which purports to demonstrate that no such advantages have accrued to United. [140]

Conclusion

653. The wholesale distribution system for wines constitutes a significant barrier to entry and expansion (Tr. 5708–09).

C. Retail Shelf Space Barrier

654. Obtaining shelf space in retail stores is critical to successful distribution of wine (Tr. 3015, 6256). The important aspect of shelf space is shelf facing. Shelf facing is the amount of space on a shelf required to display one wine bottle with its label showing (Tr. 654).

655. Fred Weibel, President of Weibel Champagne Vineyards testified:

The total battle in distribution is for shelf facings. You cannot sell to the consumer if you don't have it exposed on a shelf where the consumer can see and buy it (Tr. 654).

656. While the overall amount of shelf space allocated to wines at the retail level has increased as consumer interest in wine has grown (Tr. 673, 2008–09, 7474), gaining access to the expanded wine shelf space remains very difficult (Tr. 654, 5710–11, 10,484). Witnesses described the efforts to gain shelf space as a "battle" (Tr. 654), a "bitter fight" (Tr. 6257) and competition for shelf space as "extremely intense" (Tr. 6849). The 1976 edition of *Impact,* a wine industry trade publication, summarized the situation: "[T]he battle for inches on the retailers' shelf has never been fiercer" (CX 367Z–3).

657. Mr. Setrakian, President of California Growers Winery, Inc., testified:

One of the basic keys to the success of a proprietary case goods operation is the availability of shelf space, which is becoming a commodity in great demand because of the limitation of it. Once you gain it, you do everything you can to retain it. Once you lose it, it is very difficult to get back (Tr. 1989).

658. One indication of the constricted nature and importance of wine shelf space is the necessity of retailers to discontinue a wine item if another wine item or line is added to the shelf (Tr. 2033–34, 2066–67, 2069, 6853, 7938). And once a wine item has lost its shelf space to another brand, it is difficult to get space back (Tr. 1989, 7934–35). **[141]**

659. Although floor stacks have been used to expand the space available for retailing of wines, floor stacks for a given brand or item are limited, temporary and difficult to obtain. It is shelf space that really counts (Tr. 1085, 1990, 2031–33, 2062–63, 6257, 7242).

660. The greater the number of wine items in a brand line for which a winery can obtain shelf space, the greater the potential for development of brand recognition through shelf space exposure (Tr. 1084–85, 8608). Correspondingly, the greater the number of wine items of a brand or brands for which a winery can obtain shelf space, the more difficult it becomes for items of competing brands to obtain shelf space (Tr. 1989).

661. Eye level shelf position in a retail store is considered the most desirable (Tr. 2062).

662. Retailers decide on the shelf space and shelf facing to allocate to items of a wine brand based upon their expected movement off the retail shelf (Tr. 1085, 2061, 2068, 3011).

663. A supermarket chain's wine buyer testified that he generally does not purchase wine items unless they have already established a record of sales and that the most important factor in determining which wine items or brands to carry is case movement or turnover. The record of case movement off the retail shelf also determines whether a wine item will be dropped or retained (Tr. 2066–68, 2072).

664. The relationship between a wine brand's wholesaler and prospective retailers is a significant factor controlling the likelihood of a brand's items being placed on retail shelves (Tr. 626, 662–65, 1085, 4699, 4701, 4703, 5169, 5230; and see Finding 557, *supra*).

665. In recounting the advantages of the proposed Heublein/United merger to members of Allied, Heublein representatives represented that, with a major supplier like Heublein, the likelihood of getting greater shelf space would be increased if United's wines were distributed along with Heublein's products (Tr. 2695).

Utilization of Secondary Wine Lines As a Marketing and Distribution Tool

666. A "secondary line" of wine is generally a case goods line of a vintner which is priced lower than its more widely known or primary case goods line (Tr. 1115, 1984).

667. A secondary line of wine can be used to block out wine brands of competing vintners at the wholesale and retail levels (Tr. 1116, 1124, 1989, 2033–34). [142]

668. A secondary line of wine may be utilized to erode a competitor's relationship with its wholesale customers by offering a cheaper price to get a foot in the door with the distributor (Tr. 2033, 3244, 3246–47, 3257, 3284).

669. A secondary line of wine may be utilized defensively by a wine marketer to retain shelf space in retail outlets against other wine brands, as well as offensively to undermine competitors' wine sales and thus threaten the continued position of other branded wine items on the retail shelf (Tr. 1989, 2011–12, 2031–34).

670. In marketing Lancers, Heublein has used a secondary line of wine as a blocking brand. As stated in Heublein's Faisca Rose Wine Marketing Plan for fiscal 1972/73:

> At various corporate junctures, Quinta, Vinya and Faisca were conceived as "blocking" brands on the one hand, or as candidates which might generate control of segments of the Portuguese Rose business at different price levels (CX 129B).

671. Heublein's Vinya Marketing Plan for fiscal 1972/73 included, as part of its "Brand Philosophy":

> Vinya will be repackaged and repriced, and will be used as a brand to stave off the increasing low priced competition from other imported rose wines that are making inroads in various parts of the country (CX 352G).

The Plan called for lowering the FOB price (CX 352M, U) and forecast negative gross profits for the brand (CX 352U, V). The plan was "to use Vinya to fight the lowest priced roses . . . " (CX 352W).

672. Petri and Parma, also known as Petri's Parma (Tr. 1093), are two secondary wine brands of United (Tr. 1116–17, 1985).

673. From March 1977 to at least December 1977, United offered Petri or Parma table wines at FOB prices below cost to wholesalers in Florida, Virginia, New York, Massachusetts, Rhode Island, Missouri and Wisconsin (RX 1147A, F; CX 354; Tr. 1090–92, 1187–91, 3241–44, 3248, 3284, 4428–30).

674. The record contains illustrations of four winery competitors of United that lost wine sales as a result of their inability to meet the Parma or Petri FOB table wine prices on a profitable basis during

the period in 1977 that Parma and Petri were being sold below cost (Tr. 1092–93, 1986–87, 3246–47, 4231). [143]

D. The Advertising and Brand Recognition Barrier

1. Brand Recognition

675. From the mid-1960's to the present, as consumption of wine has increased, the brand marketing of bottled wines has received increased emphasis by wine suppliers in the United States (Tr. 7796, 9839; CX 360N).

676. Consumers of wine are brand conscious, particularly frequent users who are brand followers and tend to be brand loyal (Tr. 2977, 7525, 9928).

677. A 1972 *Time* magazine study of wine buying in six major metropolitan markets found that the most important consideration for a purchaser of wine is brand reputation. The study noted: "An advertised brand with a quality image has its greatest sales potential in this primary market" (RX 479Y).

678. The 1977 edition of *Impact,* a wine industry trade publication, described 1976 as a year in which "established brand franchises showed their importance" and a year in which "establishment of new brands was extremely difficult" (CX 366Z–10). *Impact* further noted that "most large bulk-oriented wine producers without established brands" had a poor year in 1976 (CX 366Z–5).

679. Vintners prefer to engage in the proprietary (*i.e.,* branded) case goods business in contrast to private label (Tr. 1016, 1950, 5170, 7796, 7799). Bulk wines are not profitable for wine producers (Tr. 7799, 9527).

680. The goal of brand marketing is product differentiation (Tr. 8556–57; CX 125E, 335).

681. Establishing and maintaining a favorable brand image of a line of wines is vital in order (a) to create and maintain consumer awareness and demand and (b) to attract and retain wholesalers and retailers (CX 97U, Z–6, 114F, 116B, J, 125F, H, Q, 188K, 192A–B, D, F–H, 231F–G, Z–25, Z–44, Z–45, Z–47, Z–51, Z–53, Z–55, 326, 367W, 393C, L; RX 251D, B, G, 400A–D, 424A–C, 461A–C, 479Y, 492, 933M; Commission Physical Exhibits Y thru Z–2; Tr. 465, 511, 657, 767, 1871, 1983, 2095, 3038, 3367, 4026, 4883, 5239, 6364–65, 7490, 8311–12, 8608, 8555–56, 8743–44, 9839).

682. Wholesale distributors of wine are reluctant to take on wine lines which have not achieved some brand recognition. They do not have time to do pioneering to get new products accepted (Tr. 3368–69).

683. Brand recognition makes it easier to get shelf space and shelf facings (Tr. 657, 1086). One long-time California vintner (Tr. 618–19) testified, "The better known your brand is the easier it is to get a shelf facing. If [144]it is a name brand, retailers know it is going to move and that is the proof of the pudding as far as the retailer is concerned" (Tr. 657).

684. Following the acquisition of United by Heublein, efforts were made to emphasize the promotion and marketing of United's products as brands rather than as commodities (Tr. 4464, 7778, 7796, 7799).

685. Strong brand recognition in the wine business takes an exceptionally long time to establish. Robert Setrakian, President of California Growers Winery, a new entrant in the proprietary or branded wine case goods business, testified that he expected his branded label, which had been introduced in 1973 or 1974, to "take a minimum of another fifteen years" to establish with "long-term continuity" (Tr. 1948, 1983, 1999, 2029).

Mr. Setrakian added:

> If one were to check into the marketplace, you would find out that the well-established brands, whether it be Gallo or Christian Brothers or any of them, have been in the marketplace for well over 35 years (Tr. 2029).

686. A brand name which is identified with a long tradition of winemaking is a substantial asset. Brand association with a tradition of winemaking is a fact which is emphasized in wine marketing to wholesalers, retailers and consumers. This helps in developing consumer acceptance (RX 378A, 384A, 422, 457, 486, 494A).

687. A "wine item" generally refers to any size or any variety of wine product. It encompasses the same products sold in different sizes and different varieties sold in the same size (Tr. 2024, 7895–96).

688. A "line extension" is a new product item sold under an existing brand name, *e.g.,* Lancers White wine [Vinho Branco] (Tr. 3759).

689. Once brand recognition of a line of wines is achieved, wine producers seek to capitalize on the brand recognition by line extensions under the brand name (Tr. 3759, 7834–35, 8557; CX 361P, 366Z–5, Z–7, 367Z, Z–2).

690. Among the long-term objectives of the 1972/73 Lancers Marketing Plan was to "[t]ake advantage of line and size extensions to maintain and increase momentum (Increased share)" (CX 125G). [145]

691. A Heublein February 1970 intracompany memorandum reported: "Long range plans call for line extensions of White and

Red Lancers . . . The stronger base we are able to build in the next couple of years on Lancers Vin Rose, the easier (and cheaper) it will be to introduce line extensions without corresponding increases in advertising" (CX 115A).

2. Utilization of Advertising To Create and Maintain Brand Recognition

692. Advertising is recognized by wine marketers, including Heublein, as a very important factor in creating and maintaining wine brand recognition and in increasing wine brand sales (Tr. 1983, 3038, 3367–68, 3690, 3699–3700, 3715, 3756, 3763–64, 3804, 8608; CX 49M, 51H, 52H, 97Z–12 thru Z–16, 98B, 99K, 102C, F, 103K–L, 116K, W, 125F–H, Q, 129L, N–O, U, 231E, Z–20, Z–22, Z–23, Z–25, Z–33, Z–42 thru Z–49, Z–54, Z–60 thru Z–63, 256Z–14, 352C, I, Z–1, 353B, 360M, 585D, I, K, P; RX 251D, F).

693. Image advertising is widely utilized in the marketing of wines (CX 466; RX 348A–B, 373, 406, 425, 457A–B, 462A, 464, 468, 566). Advertising can be a central factor used in the creation or enhancement of a wine brand's image (CX 97K, Z–6, 98B, 99B, K, M, 116K, 125E, F, Q, 231F–G, Z–25, Z–44, Z–45, Z–48 thru Z–50, Z–53 thru Z–56, 256Z–59; Tr. 8743–44).

694. The Italian Swiss Colony Marketing Plan for fiscal 1970/71 cited as a marketing strategy for its table wines: "Increase consumer awareness and quality image of ISC versus Gallo, especially for products where no discernible difference exists, through 'line' advertising" (CX 231Z–25).

695. Heublein's "Harveys Marketing Plan Summary," dated April 23, 1970, notes that it will rely primarily on advertising and merchandising to position "Harveys Bristol Cream away from the sherry or cream sherry market in terms of image," adding however that "we still must consider this market in terms of potential and competition" (CX 99K, M).

696. Notable examples of substantial advertising expenditures to create brand recognition for a wine product are the Lancers and Blue Nun brands (Tr. 3368; CX 125Z–7, 128, 366Z–13, 379D).

697. Advertising has been an important factor in creating and maintaining a high profit margin for the Lancers and Harveys products marketed by Heublein. Both products, backed by substantial advertising, have achieved product differentiation and premium prices in part through the creation and maintenance of recognized brand images (CX 97K, 99A, J, K, M, 114E–G, 116B, J, L–M, 125E–G, 218Z–289, Z–290, 441B; Tr. 3690, 3699, 8743–44; RX 251C, D, G). [146]

698. Heublein's 1972/1973 Marketing Plan for Lancers called for

continued "heavy spending" on Lancers in order to "reinforce our image and story to the consumer" (CX 125F). Shorter length commercials were preferred because of already high Lancers Rose consumer awareness but continued "need to reinforce our image" (CX 125Q).

699. Heublein's Vinya Marketing Plan for 1972/73 stated: "In order to build Vinya into a volume brand, it is essential that significant advertising dollars are available to build the necessary consumer awareness and demand in our major markets, and to insure distributor and trade support" (CX 352I).

700. Wine suppliers whose wines already have established brand recognition enjoy an absolute cost advantage in advertising over firms without established wine brand names (Tr. 5718–19, 5738–39).

701. Richard Oster, President of United from September 1970 until September 1973 (Tr. 7778), judged that, for the long-term good of United's wine business, the company could more profitably spend its money in advertising, which has a cumulative effect, than in price promotions (Tr. 7859, 7863–64, 7926–27). Mr. Powers, Chairman of the Board of United, also believes wine advertising benefits extend into the future (Tr. 9902).

702. Advertising is also required to maintain substantial sales of already established brands (Tr. 7944, 9322, 9608; CX 111A, 114F).

703. The necessity to advertise a branded wine increases as competing brands of wine are advertised (Tr. 8342, 8354–56, 9608; CX 125F, Z–17).

704. The fiscal 1972/73 Lancers Marketing Plan strategy was to "continue to spend at a high level behind advertising and promotion" in order to "dominate the 'noise level' among wine advertisers" (CX 125F).

705. Since other wineries provide advertising support to their brands, it is also necessary for United to cultivate retailers through commitments of advertising support for United's brands in order to help move the product out of the store. Although an attractive promotion may encourage a retailer to carry a wine brand, it is still necessary to advertise (Tr. 8355–56).

706. Wholesalers' salesmen have priorities in devoting time to the wine brands they represent. A salesman generally gives preference to the brands carried exclusively by the wholesaler. Next, he is motivated to sell the wines that are most attractive to the retailer by virtue of fast movement off the retail shelf (Tr. 3324–25, 3366–67). [147]

707. Brand advertising is an important factor in creating movement of wine off the retail shelf. Consumers are influenced to

purchase wine brands by brand advertising (Tr. 654, 656, 660, 767, 772, 1088, 2232, 2853, 2859, 3011, 3367, 8356, 9838).

708. A commitment by a wine supplier of advertising support for a brand is an important factor in getting wholesale distributors and retailers to carry the brand (Tr. 2994, 3010–11, 3366–68, 4206–07, 6849; CX 97Z–27, 120S–T, 125F). Advertising in trade journals may also influence purchases (Tr. 656).

709. In states with pricing restraints, such as affirmation laws, price posting requirements or minimum markup requirements, large wine companies with resources to advertise can be much more effective than where there is an unrestrained market (Tr. 1055–56).

710. In states which control the sales price of wine, advertising is more effective in generating wine sales. If pricing is one of a supplier's tools of selling and he does not have advertising money to spend, the inability to use pricing as a selling tool makes competitors' advertising all the more effective. For example, Ohio fixes the minimum price, called a "floor", at which a winery can sell to the wholesaler, the minimum margin at which the wholesaler must sell to the retailer, and the minimum margin or markup of the retailer to the consumer. A vintner that tries to break into such a market without advertising money to spend is deprived of price as a selling tool. If competitors advertise their wine brands in a state such as Ohio, the winery without advertising funds cannot lower its price to save its sales volume against competitive inroads induced by the advertising (Tr. 1047–48).

711. In states with affirmation laws, the vintner is compelled to sell to wholesalers at the lowest price at which the wine product is sold anywhere in the United States. Therefore, advertising is more effective even in non-affirmation states in generating sales and taking business away from non-advertisers of wines who cannot drop price any lower and remain profitable (Tr. 1053–56).

712. United Vintners has utilized "line advertising" to promote all the products of different wine types under the same brand name. The FY 70/71 Italian Swiss Colony Marketing Plan states the "rationale" for line advertising:

> Line advertising provides an umbrella for products under the ISC Brand which have no discernible difference from similar Gallo items. The objective is [148]to plant an image of modernity and quality in the consumer's mind . . . (CX 231Z–45).

713. Heublein's Lancers Marketing Plan for fiscal 1972/73 also recognized the advantages of line advertising when enunciating the long term strategies of the Lancers brand:

Take advantage of line concept in advertising, merchandising and sales promotion. (Some cannibalization, but great economies and more realistic.) (CX 125G)

3. Merchandising and Packaging

714. "Merchandising" materials in the wine business generally refer to retail point-of-sale or retail display materials used to attract consumers' attention to a branded product (Tr. 632–33, 2063, 7858, 8765).

715. Such merchandising is utilized in wine brand marketing as a tool to establish and maintain wine brand recognition (CX 99C, K, T, 111B, 115B, 116E, 125Z–6, Z–26, Z–27, 129L, V, 236F, 352P, Z–2, 256Y, Z–14, Z–15, 569C–J; RX 251E, M–N).

716. It is a form of advertising, although distinct from media advertising (Tr. 2284, 6213, 6650; RX 438).

717. The quality and quantity of retail display materials available from a vintner is a factor which wholesale distributors weigh in deciding whether or not to take on a wine or wine line and how strongly to support the vintner's wine products viz-a-viz other wine products in the wholesale house. Display materials also motivate retailers to buy a vintner's brand(s) (Tr. 3324–25, 7508–09, 8305).

718. Packaging (including bottle size and design) and labeling changes are another form of nonprice competition used in wine brand marketing (CX 97Z–27, Z–28, 99C, T, 111B, 125Z–35, 129W, 231F, Z–25, 242D, 256Z–17, Z–26, Z–34, 352W, 569C–J).

719. Packaging and labeling are very important in the sale of wine (Tr. 3325, 3789, 4207, 6201, 6799, 7490, 7509, 9617; CX 231F–G, 352G, 360P, 393C–D).

720. Packages go out of style and more contemporary designs are fashioned to make wine products attractive (Tr. 3789, 7484–85, 7490). Different bottle sizes are used to achieve variable retail pricing per ounce of wine (CX 256Z–61). [149]

721. Label designs are used in wine brand marketing to differentiate products (Tr. 7614–15).

722. Most major competitors, including United and Heublein, Gallo, Almaden, Christian Brothers and Paul Masson, restyle their packaging (Tr. 3789; CX 231F, 352G, 367Z–2).

723. Brand advertising, including merchandising, works together with packaging in wine brand marketing to establish and maintain brand recognition at the retailer and consumer levels (CX 97Z–27, Z–28, 115A–B, 116B–C, 129U–W, 231F–G, Z–46, Z–48, Z–50, Z–54 thru Z–56, 360P, 393C–D).

4. The Necessity of High Advertising Expenditures Constitutes a Barrier to Entry

724. As testified to by United's recent Vice President of Marketing, a firm wishing to enter or expand in the wine industry so as to take a share of the market away from United or Gallo would have to engage in advertising (Tr. 8441, 8616–17).

725. Among the factors contributing to the failure of Montcalm Vintners, Inc., a new winery entrant, was inadequate advertising support of the company's brands (Tr. 5154–55, 5175–76, 5185).

726. Korbel Winery, a well-established sparkling wine producer tried to expand into the production and sale of table wines, but failed due to inadequate advertising support for its table wine line (Tr. 2208, 2230–33, 2271).

727. Advertising support for national introduction of a new wine product is costly (Tr. 2146–48, 2223, 2232–33, 3705–08, 3710–11, 5154–55, 7963, 8023–24; CX 201A, 585Z–2, Z–34).

728. Generally, in order to establish a new wine brand, it is necessary to spend more on advertising than for an established brand to the point that a firm entering the market must spend twice the advertising dollars of its competitor to take a share of the market away from that competitor (Tr. 8432–33; CX 115B).

729. The enormity of that undertaking in connection with competing for a portion of United's market share is reflected by the public statement made a little over a year after the merger, in May 1970, by Stuart Watson, Chairman of the Board and Chief Executive Officer of Heublein:

> I think our [advertising] effort in national magazines such as Life, Time and Newsweek, on TV and in newspapers probably rates as the most intensive and extensive campaign of wine promo- [150]tion ever undertaken by a single company in this country (Tr. 5015–16).

730. A new firm spending the same dollar amount as industry leaders for advertising must spread its costs over a smaller volume of sales. A company attempting to enter or expand in the wine industry, therefore, suffers an absolute cost disadvantage in advertising in comparison to industry leaders (Tr. 5719–20).

731. A new line would have to be supported by "front load" or "investment spending". This means advertising expenditures at such a high level in support of a wine product over an initial period of time that the margin on the product sold would not recover current advertising expenditures. The product would have negative earnings on the assumption the investment would be recovered on later sales (Tr. 3705–08, 3710–12; CX 129U).

732. There is no certainty that advertising investment spending for a wine product will ever be recovered. Advertising investment spending is a risky proposition (Tr. 3712; CX 585Z–42).

733. In Heublein's Faisca Rose Wine Marketing Plan for Fiscal 1972/73,[26] it was estimated that the introductory media advertising campaign for national rollout of Faisca would be $1 million and that the cost of the media advertising campaign to sustain Faisca would be approximately $925,000 per [151]year. It was estimated that an additional $350,000 in merchandising expenses would be required for the introductory national rollout (CX 129E–G, L). For the first two years of rollout Heublein estimated that "front load" spending on Faisca, and other factors, would result in product line earnings loss for Faisca of $322,500 (CX 129P, U).

734. Lancers' advertising to sales ratios were 2.7 percent in Heublein's fiscal 1966, 10.9 percent in fiscal 1967, 11.6 percent in fiscal 1968 and 8.0 percent in fiscal 1969 (CX 135G).

735. Between Heublein's 1966 and 1972 fiscal years, Lancers' annual advertising expenditures rose from $75,000 to $2,160,000 (CX 125Z–16), and the brand earned direct profit of $4,276,000 on net sales of $11,853,000 in 1972 (CX 125Z–7). This represents an advertising to sales ratio of over 18 percent. For fiscal 1970/71, Heublein projected spending $4.44 per case of Lancers on media advertising (CX 116I).

736. Harveys' advertising to sales ratios were 17.9 percent in Heublein's fiscal 1966, 15.1 percent in fiscal 1967, and 15.6 percent in fiscal 1968 (CX 135G).

737. The following charts depict advertising to sales dollar ratios for a number of Heublein and United products. The charts provide such ratios in a number of ways, including and excluding excise taxes, and reflecting in some instances marketing expenditures which include advertising, merchandising and packaging. Promotional expenses are also treated in varying manners to take into account HUV's contentions that promotional expenses are really price post-offs. HUV object to the exclusion of excise taxes from sales contending that the total price includes the excise tax. I disagree. Taxes are imposed upon sales or withdrawals but do not reflect the

[26] HUV have objected to the reliance upon projected or planned advertising figures which, they claim, do not necessarily evidence actual advertising expenditures. However, marketing plans and budgets are very carefully prepared documents produced and maintained in the regular course of business and approved at the highest levels. Corporate expenditures, including advertising expenses, are matters concerning which detailed and exact business records are maintained. To the extent HUV may have wished to overcome reliable documents reflecting advertising expenses introduced by complaint counsel, it was incumbent upon HUV to have produced and authenticated more reliable documents. This they have not done. Self serving letters submitted to complaint counsel (*e.g.*, CX 330A–B) do not overcome such reliable documents.

The same ruling applies to data supplied to the Commission by HUV during the course of the investigation of this case to the extent that HUV now assert the submittals are incorrect.

return to the seller. The appropriate sales figure is one which excludes excise taxes. [152]

SEE *IN CAMERA* ADDENDUM [153]

SEE *IN CAMERA* ADDENDUM [154]

ADVERTISING:SALES RATIOS
UNITED VINTNERS
(FY 72 (budgeted)(CX 256Y))

PRODUCT	MEDIA AD: SALES RATIO 36/	MEDIA AD: SALES RATIO 37/	AD:SALES RATIO (NON-PRICE MARKETING) 38/
ISC (excluding Bali Hai)	5.8%	6.0%	7.0%
Bali Hai	9.5%	9.8%	11.3%
Inglenook	8.7%	10.0%	13.2%
New Products	22.8%	26.2%	30.9%

36/ Excluding excise tax.

37/ Excluding excise tax and sales promotions from sales.

38/ Combining budgeted non-price marketing expenditures for advertising and merchandising, excluding excise tax and sales promotion.

[155]SEE *IN CAMERA* ADDENDUM [156]

SEE *IN CAMERA* ADDENDUM [157]

The advertising:sales ratios reproduced above are particularly significant in that they show that Heublein engaged in much higher advertising in proportion to sales[44] than United and that the ratios for new products is twice as much, and more, as those for established products.[45]

738. The fact that a fixed amount of advertising is being used for a product which has an increasing number of cases being sold does not dilute the impact of the advertising to the consumer (Tr. 3763–64). Therefore, the absolute amount of dollars spent by a wine

[44] Heublein's advertising:sales ratios for wines are comparable to the 15.7 percent considered high in *General Foods Corp.*, 69 F.T.C. 380, 434 (1966), *aff'd*, 386 F.2d 936 (3d Cir. 1967).

[45] In addition to the data for "New Products", the ratios given for Lancers Red and Jacare reflect new product expenditures.

marketer for a brand is significant, independent of the advertising to sales ratio in evaluating advertising as a barrier to competition (Tr. 5724).

739. Major competitors in the wine industry, including Heublein, United, Gallo, Paul Masson, Almaden, Taylor, Christian Brothers and Mogen David, all advertise their brands nationally (Tr. 4887, 4889–90, 7620–21, 9830; CX 216A, 379C, D, 444–45, 579C–D).

740. Major media advertising such as network and spot television and radio, as well as print media, are used by a substantial number of wine marketers, including Heublein and United (CX 97Z–12, Z–32, Z–35, 98J, 99K, 100C, 102C, F, 111B, 115A, 118A, 119C, G, 120C, F, 125F, I, L, T, 201A, 216A, 231Z–60 thru Z–62, 239D, 240E, 241E, 242E, 243E, 300C thru M, 367Z–17, 379C thru U, 444–45, 472A–B).

741. In 1970, $30.6 million was spent in wine media advertising. By 1976, the figure had more than doubled to $63.7 million (CX 300B, 379B; Tr. 3726–33).

742. In 1976, each of the leading firms in the wine market,[46] with the exception of Guild, spent in excess of $1 million in advertising. Heublein topped the list with $16,982,977 (including HMS Frost) and Gallo followed with $13,411,227. National Distillers spent $2,101,595. Mogen David and Franzia combined for $1,269,184. Seagram spent $2,846,242 and Taylor (Coca-Cola of Atlanta) spent $1,933,816. Guild spent $686,530 (CX 379K–L). [158]

743. In 1976, estimated total expenditures for media advertising in magazine, broadcasting (television and radio) and outdoor by wine marketers was $62,017,251. Heublein's estimated wine advertising expenditures of $16,982,977 (including expenditures for HMS Frost) in that year accounted for 27.4 percent of total wine advertising in these media (CX 379L).

744. Eight companies (Gallo, Heublein, National Distillers, Guild, Mogen David, Taylor, Franzia and Seagram), which were the wine industry leaders in 1972 (CX 373K), accounted for 73.1 percent in 1970 and 66.0 percent in 1971 of total wine advertising expenditures in magazines, radio, television and outdoor media (CX 300B, K–M). In 1976, the same eight companies (Taylor having been acquired by Coca-Cola of Atlanta) accounted for 58.4 percent of all wine advertising expenditures in magazines, radio, television and outdoor media (CX 379K–L; Tr. 3726–33).

745. In 1970, estimated percentages of total United States wine advertising expenditures (excluding newspapers), by type of media utilized, were as follows: magazine, 24.4 percent; outdoor, .6 percent;

[46] These are the eight leading firms as of 1972.

spot television, 41.4 percent; network television, 20.6 percent; spot radio, 12.8 percent; and network radio, .2 percent (CX 300B; Tr. 3726–33).

746. In 1976, estimated percentages of the total United States wine advertising expenditures, by type of media utilized, were as follows: magazine, 12.6 percent; newspaper, 2.7 percent; outdoor, 1.0 percent; spot television, 41.1 percent; network television, 27.0 percent; spot radio, 12.3 percent; and network radio, 3.3 percent (CX 379B; see also Tr. 3726–33).

Conclusions

747. Advertising and other forms of non-price competition such as merchandising, packaging and label design significantly contribute to establishing and maintaining brand recognition in the wine industry.

748. Wine companies with established brands doing a substantial volume of business may enjoy absolute cost advantages in advertising their wine brands.

749. An entering or expanding firm in the wine industry has an absolute cost disadvantage with respect to advertising by virtue of the brand recognition of established competitors, large and small, achieved in part through the accumulated effect of advertising and other non-price marketing tools.

750. If the new entrant or firm desiring to expand its wine market share wants to compete on a par in terms of advertising with a firm with the established brands, it has to spend more than the established brand due to the accumulated recognition of the established firm's brand(s). [159]

751. Heublein, as one of the leading marketing and advertising firms in the United States, adds the capability of significantly increasing advertising and other merchandising expenditures in support of United's already well-established brands. This would accentuate the barrier to entry and expansion associated with the accumulated brand recognition of United's products. By May 1970, Heublein had already taken giant steps to accomplish this (Finding 729, *supra*).

E. State Laws and Regulations

752. State laws and regulations regarding wine are voluminous and complex and vary widely from state to state (*e.g.*, CX 289; Facts Submitted for Official Notice, dated May 2, 1978 and subsequently noticed without objection; Tr. 3028, 7181).

753. An August 1972 publication of The Wine Institute, the most important industry trade association, states:

> Distribution methods within the states vary radically.
>
> * * * * * * *
>
> So complex, in fact, are wine-selling restrictions among the states that it is difficult for vintners to establish national distribution. Many concentrate on selected markets, for which they have specifically designed their business operations. Interstate trade barriers and non-uniform wine laws and regulations gradually are being corrected, but progress has been slow (CX 308Z–1).

754. Mr. Serlis, former President of The Wine Institute, described the regulation of the wine industry across the country as a "hodge-podge" that makes it extremely difficult to do business (Tr. 576).

755. One of the reasons the McKesson wholesale operation is decentralized is the complexity of state regulations (Tr. 7181, 7271).

756. Even Heublein found it easier simply to avoid "the maze of laws" concerning entry in Kansas by not seeking to introduce its Faisca Rose wine in that state (CX 129D).[47] [160]

757. An Italian Swiss Colony advertisement represents that not all wine varieties are sold in every state, due in part to various state regulations (CX 333E).

758. Heublein represented to the Federal Trade Commission that it was important even for a winery the size of United to obtain a partner having "management and marketing expertise" and "knowledge of the highly complicated, comprehensively regulated alcoholic beverage business" (CX 327Z–5).

759. State laws that limit the alcoholic content of wine make it more difficult for a winery to operate because the laws vary from state to state. Florida, for example, has a tax penalty for wine with more than 17 percent alcohol (Tr. 1049–50).

760. Affirmation laws make it harder to enter a market and favor the dominant brands (Tr. 1053–55; Findings 709, 711, *supra*).

761. Many states have laws governing the resale price of wine. In Ohio, for example, the state fixes the minimum price at which a winery sells to a wholesaler, the margin at which the wholesaler can sell and the margin at which the retailer can sell (Tr. 1046–47).

762. In a fair trade price posting state, a vintner loses freedom of pricing and discounting (Tr. 1046).

763. In some states, the vintner posts the retail price. In other states, the distributor posts the retail price. The posted retail price for a winery will vary from state to state (Tr. 3272–75).

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[47] Kansas' ranking as "a very poor wine consuming state" was an additional factor in not seeking to sell in that state (CX 129D).

764. Some states permit only periodic price changes. Massachusetts has such a law (Tr. 7844, 7973).

765. It is more difficult to get distribution in control states than in open states (Finding 547, *supra*). It is necessary to make a separate application for each product a wine company wishes to have listed in a control state (Tr. 4217, 4263).

766. Some states require submission of labels for approval. Some require the submission of the wines themselves for analysis and approval (Tr. 1050).

767. To obtain a listing in Pennsylvania, each wine, type and size must be approved by the state. The application for a listing is made for a flavor type and a particular size and each application is reviewed separately (Tr. 9937).

768. Federal and state taxes vary with the alcoholic content of the wine. Federal taxes differ from state taxes. Taxes on wine differ from taxes on spirits. Taxes on wine vary from state to state (Tr. 7291–92). [161]

769. Wine and spirits prices vary from state to state depending on the various state tax laws and whether the markup structure is fixed by state regulation (Tr. 7254). Wine prices in a state also vary over time as state taxes and other variables change (Tr. 7259).

F. New Entrants in the United States Wine Industry Have Been Small Local Producers

770. Mr. Louis Gomberg, a paid consultant and witness for Heublein, prepared an exhibit (RX 1176A–H) showing "De Novo Winery Entrants" for the period 1960–76. Of 255 entrants listed during the 1960–1976 period, 221 were characterized by Mr. Gomberg as "very small, total capacity to 100,000 gallons." Mr. Gomberg further identified 29 of the new entrants as "small, total capacity 100,001 to 1,000,000 gallons." Four other new entrants were described by Mr. Gomberg as "medium, total capacity 1,000,001 to 5,000,000 gallons." Of all the entrants, one was identified as "large, total capacity over 5,000,000 gallons" (RX 1176A–H).

771. The exhibit prepared by Mr. Gomberg, however, does not accurately reflect the size and nature of new entry into the wine industry. The capacities listed do not reveal production or production capacity; they refer only to storage capacities and count an empty tank as much as a filled container. Thus a new entrant may take over an existing facility, but the storage capacity of the acquired winery does not reflect the production goals or achievements of the new entrant (Tr. 1741, 1753–54, 1757–58). Further, a winery given a permit to produce wine might actually produce none. This condition

could continue for two years before the winery's basic permit would be subject to cancellation under provisions of the Federal Alcohol Administration Act.[48] Nevertheless, the winery would be carried on RX 1176A–H as a new entrant (Tr. 1791–92, 1912–13).

772. The witness relied very heavily upon the Wines and Vines Directory, a wine industry publication, in preparing the exhibit. That directory listed capacities for most wineries. While the great preponderance of the wineries in the "very small" category had capacities substantially below 100,000 gallons, with most apparently below 10,000 gallons, Mr. Gomberg nevertheless set up the category with a 100,000 gallon cut-off (Tr. 1751, 1886–88, 1893–1904). The witness conceded that a sample check of the "very small" new entrants showed that the vast preponderance were insignificant in terms of size (Tr. 1903–04). After an attempt to avoid answering the question, the witness also conceded that some of the "very small" entrants, less than 50 percent, were retirement, hobby or part-time wineries (Tr. 1904–12). [162]

773. The one "large" new entrant identified by the witness was California Mission Wines, Inc. (RX 1176E). This company, however, is a bulk wine producer with no brands and no bottling capacity (CX 459E).

774. The four "medium" wineries were The Monterey Vineyard, Noble Vineyards, Papagni Wine Co. and Bronco Wine Co. (RX 1176D–F). The Monterey Vineyard failed and was sold to Coca-Cola of Atlanta on November 3, 1977 (Tr. 363–65). Noble Vineyards is a bulk wine producer only (CX 459E). While listed as having entered in 1972 (RX 1176D), as of January 1978, the witness could not say that company had actually marketed any wine (Tr. 1782–83).

775. The storage capacity of Papagni Wine Co. is 3,000,000 gallons (CX 459B). Bronco Wine Co.'s storage capacity is 1,000,000 gallons (CX 459B). There is no record data as to the production or profitability of Bronco Wine Co. or Papagni Wine Co.

776. During the period 1968 through 1976, there have been 105 *de novo* California "entrants" into the wine industry, which account for 3.4 percent of total California wine industry capacity in 1976 (CX 459A–E).

777. Between December 31, 1960 and December 31, 1976, total non-California winery storage capacity, including capacity both of bottled and bulk wine companies, grew by 38,168,000 gallons (RX

[48] For example, the witness conceded that he did not know whether A. Fillippi Winery, listed as a "small" entrant in 1975 (RX 1176F) had produced any wine "in the two years since they were authorized to produce" (Tr. 1781).

660). In the same time period, comparable California winery capacity grew by 417,107,000 gallons (RX 659).

778. California companies thus accounted for 91.6 percent of the total growth in domestic wine storage capacity of bulk and bottled wine companies during the period December 31, 1960 through December 31, 1976. California wine companies accounted for 93 percent of the growth during the period December 31, 1968 through December 31, 1976 (RX 659–60).

779. The ten largest California wineries plus three major bulk producers accounted for 78.4 percent of the total increase in California winery storage capacity between December 31, 1968 through December 31, 1976 (CX 458A–B).

780. Two ambitious attempts to enter the production and marketing of bottled and branded wine on a significant scale since 1970 are California Growers Winery and Bear Mountain Winery. Both of these entrants were successors to bulk wine operations and have continued to sell bulk wine while attempting to develop a case goods operations (CX 409, 458A; Tr. 1948–49, 1956–58, 1965, 1980, 1998–99, 2014, 9767–68).

781. California Growers Winery has never earned a profit from its branded case goods sales in the seven years during which it has endeavored to establish itself (Tr. 1958–59). [163]

782. Bear Mountain Winery began producing bottled wines under its own labels in 1973 or 1974 (Tr. 9767). It had sustained losses in excess of $31,000,000 as of January 1978 (Tr. 1996, 7634, 9505–06). Its tax-paid withdrawals of wine have declined over the period 1975 through 1977 (Tr. 9505). Within the last year, Bear Mountain has been sold to the Jean Labatt Company of Canada (Tr. 9504).

783. The record, therefore, shows that, while there have been a number of small *de novo* entrants into the wine industry, there have been no successful, significant *de novo* entrants.

G. There Are Substantial Barriers to Entry in the Wine Market—Discussion and Conclusions

A barrier to entry is an arrangement or condition in an industry that impedes free entry. A barrier to entry may also be referred to as a "barrier to effective competition." *The Budd Co.*, 86 F.T.C. 569, 577 (1975). The concept encompasses a barrier to expansion (Tr. 5701–03). It is not necessary that there be many or a particular number of barriers. Cases in which barriers play a role may involve only one or two barriers. See, *e.g., General Foods Corp.* v. *FTC*, 386 F.2d 936 (3d Cir. 1967). The issue to be resolved is whether there is in fact a barrier to entry. Such a barrier may exist because of a single

situation or because of a combination of circumstances. Here, the record shows a number of substantial barriers to entry.

Entry or expansion, for purposes of Section 7 analysis, refers to an "effective competitor" making "substantial sales" in a relevant (here national) market. See, *Warner-Lambert Co.*, 87 F.T.C. 812, 880–81 (1976). See also, *Missouri Portland Cement Co.* v. *Cargill Inc.*, 498 F.2d 851, 857 (2nd Cir.), *cert. denied*, 419 U.S. 833 (1974) (court's analysis assumes entry the size of the acquired company); *United States* v. *Falstaff Brewing Corp., on remand*, 383 F. Supp. 1020, 1021 (D.R.I., 1974) (court's analysis assumes entry at "an acceptable level of sales"); *United States* v. *Phillips Petroleum Co.*, 367 F. Supp. 1226 (C.D. Cal. 1973), *aff'd*, 418 U.S. 906 (1974) (court's analysis assumes a major market entry).

As most recently evaluated by the Commission, the question is whether there is a barrier to that level of entry which approaches that of the industry leaders or which is sufficient to challenge the dominance of industry leaders. *Freuhauf Corporation, Inc.*, 91 F.T.C. 132, 232 (1978).

While it has been possible for a number of entrants to produce and sell wine in small quantities, such endeavors have no significance in terms of competition in the relevant markets. [164]

1. The Long Payout Period Characteristic of Investment in the Wine Industry Constitutes a Significant Barrier

The long period of time during which a firm must pay money out before receiving a return is a significant barrier to entry in the wine industry. Three aspects of the industry contribute to this long payout period. First, new vineyards do not produce grapes at capacity for five to six years after planting. Second, because of the nature of the production process, wine is not placed into distribution channels until at least six months to as long as ten years after the grapes are first picked. Third, it takes a great deal of time to create consumer demand for a brand of wine. The expenditures necessary to create brand recognition must be made up front and there is no way to predict when to expect a return. A return on investment will not begin until there is an established demand for the product.

Long lead times significantly reduce the likelihood that entry into a particular industry will be economically feasible. *FTC* v. *Atlantic-Richfield Co.*, 549 F.2d 289 (4th Cir. 1977). The delay involved in establishing a business to the extent necessary to receive a return is, therefore, one of the obvious factors that potential entrants consider. See *Missouri Portland Cement Co.* v. *Cargill Inc.*, 498 F.2d at 864; *United States* v. *Black & Decker Mfg. Co.*, 430 F. Supp. 729, 762 n. 64

(D. Md. 1976). In *Fruehauf Corporation, Inc.,* 91 F.T.C. at 225 n. 16, the Commission found that a time component of four years for entry was "obviously a barrier." *Accord, RSR Corp.,* 88 F.T.C. 800, 888 (1976) (three years).

This record shows that a varying but substantial number of years is required from the time a company first seeks to establish a source of grapes until its wine is ready to enter distribution channels. In addition, substantial time is required to create consumer preference for a brand. Clearly, the overall length of the payout period for entry into the wine industry compounded by the addition of time it would take to become profitable constitutes a high barrier to entry.

2. Capital Requirements Constitute a Significant Barrier

The amount of capital that must be invested to develop new production capacity in the wine industry is sufficiently high to impede significant new entry or expansion. If a winery chooses to establish its own vineyards, as many have in order to assure themselves an adequate supply, it may cost $8,000 per acre, exclusive of the price of the land itself, to bring the vineyard to full bearing capacity. Beaulieu, for example, number 28 in the table wine market in 1968 with a .25 percent market share (CX 373Z, unranked in other markets), expected to be able to increase its capacity by 75,000 cases in that year because of 150 additional acres it had put under cultivation several years before (CX 207A). **[165]**

The record shows an example of where the capital outlay for production facilities alone has been $5,800,000 for 2 1/2 million gallons of capacity, a gallonage substantially below the eighth ranked firm in the all wine industry in 1972 which, with a market share of 2.3 percent had 75,953,000 gallons of wine entering distribution channels (Findings 524–26, *supra*).

An additional investment burden is the necessity of maintaining expensive wine inventories. Certain parts of the plant and equipment necessary to produce wine are used for a relatively short period of time each year. This seasonal aspect of the industry means that at least a year's supply of inventory must be maintained.

The absolute amount of capital required for entry or expansion in an industry is significant to the extent that it is "so large that relatively few individuals or groups could secure it." It is also "a rough measure of the *risk* faced by a new entrant" so that even if a company could afford it, it would be reluctant to take the risk. *Fruehauf Corporation, Inc.,* 91 F.T.C. at 224 n. 14. And see, *Jim Walter Corp.,* 90 F.T.C. 671, 761, 762 (1977) ($9 to $12 million

considered "not insignificant" or "moderate"); *RSR Corp.*, 88 F.T.C. 800, 888 (1976) ($10 million considered "significant").

The absolute amount of investment necessary to develop new capacity in the wine industry constitutes a significant barrier to entry. The investment figures in this record referred to above would have to be multiplied several times for entry on a scale sufficient to challenge the market leaders.

3. Limitations on Distribution Constitute a Highly Significant Barrier

One of the requisites for successful entry is an adequate distribution system. See, *e.g.*, *United States* v. *Falstaff Brewing Corp., on remand,* 383 F. Supp. at 1024. *United States* v. *Phillips Petroleum Co.,* 367 F. Supp. at 1246. In *United States* v. *General Dynamics Corp.,* 415 U.S. 486, 501 (1974), the Court observed that "in most markets distribution systems" are a "significant" factor in assessing a firm's competitive strength. A commercial winery seeking to grow to any appreciable size faces a very steep barrier in trying to arrange effective distribution for its products.

In most states, wineries are required by law to distribute their products through wholesalers. Wineries generally prefer to distribute their products through combined wine and spirits wholesalers because they are usually the more effective wholesalers in a given market. The fact that established wine companies distribute through major wine and spirits wholesalers demonstrates that this is the more [166]effective method of distribution. The major metropolitan markets, in which most wine is sold, generally have only a limited number of effective wine and spirits wholesalers for a winery aspiring to significant size. The number of such wholesalers has been decreasing.

The problem, however, goes beyond the limited and declining number of effective wholesalers for wine in major wine consumption areas. Whether or not they choose to exercise it, major suppliers, particularly spirits suppliers, have an undue influence over their wholesale houses so that competing products may not be taken on. This is because of the importance to the wholesalers of the major products they are handling and the fear of doing anything that might impair ongoing relationships with their major suppliers.

Effective wholesalers are reluctant to take on new lines of wines of any significance in terms of volume from anyone other than a present major supplier. A strong favoritism is inherent in the wholesaler's relationship with the major supplier. Indeed, as in *United States* v. *Wilson Sporting Goods Co.,* 288 F. Supp. 543, 555

(N.D. Ill. 1968), the incentive to treat a major supplier's products favorably "may even initiate with the dealer." Heublein and United are prime examples of major suppliers that are in an advantageous position to place new products or line extensions with their existing wholesalers to the point of filling all the wholesalers' needs and, correspondingly, to deter their wholesalers from taking on competing products. In addition to a relationship which favors present major suppliers to the detriment of new entrants, the record evidences instances where major suppliers have exercised leverage to that end.

The process of building a distribution network sufficient to gain an appreciable share of the market would be an obstacle to a new entrant or a small firm in any national consumer goods industry. In the wine industry, however, it is especially difficult to the point of constituting a significant barrier because of the limited availability of effective distributors and because of the ability of large, established firms to influence their existing wholesalers to extend distribution of their own new products to the exclusion of aspiring competitors.

Apart from the barriers to securing adequate distribution through wholesalers, it is also difficult for a new entrant to secure any distribution in a control state.

4. The Difficulty in Obtaining Retail Shelf Space Constitutes a Barrier to Entry

Obtaining shelf space, or shelf facings, in retail stores is critical to successful distribution of wine. However, it is difficult to obtain such space. A limited amount of shelf [167]space is available for wine at any given time, and it is usually necessary to displace a wine item currently on the shelf in order to expand the number of facings for another item or to obtain a facing for a new item. Large, established firms may be able to obtain more favorable and greater amounts of shelf space. Heublein, for example, represented to Allied that it was capable of obtaining greater shelf space for United's products.

High costs are incurred in obtaining shelf space. Retailers prefer to take on products only if they have established brand recognition or established sales. Brand recognition is costly to acquire. Other means of obtaining shelf space, such as promotional pricing or use of a great deal of salespower, are also very costly. See *The Procter & Gamble Co.*, 63 F.T.C. 1465, 1566–67 (1963).

Difficulty in obtaining adequate displays or shelf space, therefore, constitutes another barrier to entry or expansion in the wine

industry. See *General Foods Corp.* v. *FTC,* 386 F.2d 936, 945 (3rd Cir. 1967).

5. The Difficulty in Creating Consumer Demand for a Wine Brand Sufficient To Gain an Appreciable Share of the Market Constitutes a Substantial Barrier to Entry or Expansion

One of the requisites for successful entry into the wine business is the ability of the entrant to ensure sales by creating a preference among consumers for its particular wine products. Impressing the consuming public that products are different is important in marketing wine because wines are relatively low-priced products whose distinguishing physical features, aside from color, are not readily discernible by consumers. See *General Foods Corp.* v. *FTC,* 386 F.2d at 338; *Black and Decker,* 430 F. Supp. at 775; *Fruehauf Corporation, Inc.,* 91 F.T.C. at 227. Furthermore, some sort of pre-sale or differentiation of products is important in the sale of wine because it is often sold through self-service outlets. See discussion in *United States* v. *Lever Brothers Co.,* 216 F. Supp. 887, 893 (S.D.N.Y. 1963). *Accord, General Foods, supra.* Because of the array of wines available for the consumer's selection, the creation of the impression of product differentiation is probably more important in the marketing of wines than for most consumer goods.

Product differentiation is achieved in the wine industry primarily through brand recognition based on favorable images of quality. Successful achievement of brand recognition is a very significant factor and an indicator of competitive strength. See *General Dynamics Corp.,* 415 U.S. at 501. The [168]record shows that it is essential to establish and maintain brand recognition by projecting a favorable brand image. Brand name recognition can "prove a decisive advantage" insofar as it is likely to be transferable to new products in the same market. *Black and Decker,* 430 F. Supp. at 764–65. The record exemplifies how wine companies with established brands trade on their name through "line extensions".

Brand marketing has become increasingly important in the wine business, and all wineries attempt to associate the image of their brands with quality. The record shows that advertising is very effective in stimulating and maintaining a preference among consumers for a particular brand of wine. Some notable examples of the successful use of advertising in the wine business are Italian Swiss Colony, Harveys and Lancers. Advertising also has been used effectively as a means to create brand recognition and preference sufficient to enable marketing high margin wine products such as Lancers and Harveys.

Consumer preference for certain brands in the wine industry may also stem from a "long history of industry dominance." *General Foods,* 386 F.2d 936 at 945. United and Gallo enjoy this advantage. Brand recognition may also be generated through the use of other non-price forms of promotion such as merchandising, packaging and labeling.

"[C]ommon sense" indicates that advertising has a significant impact in markets of a consumer oriented nature. *Black and Decker,* 430 F. Supp. at 752. The principal way to gain an appreciable share of the market within a reasonable period of time is through the use of "mass advertising and market promotion." See *General Foods,* 386 F.2d at 938. The record in this case shows that advertising is a major competitive weapon in the wine industry. New firms and small firms that seek to grow must somehow find a way to overcome the existing "noise level" of advertising to capture the attention of consumers for their brands.

New firms and small firms attempting to gain an appreciable share of the market operate at a disadvantage with respect to advertising since firms with larger established brands enjoy absolute cost advantages. As a general rule, "distinct advantages" in advertising and brand loyalty "stem from nationwide marketing." *United States* v. *Phillips Petroleum Co.,* 367 F. Supp. at 1245.

One absolute cost advantage stems from the cumulative effect of advertising. The effect of a given advertising expenditure by an established firm is greater than the effect generated by the expenditure of the same amount by a firm with a less established brand. A new entrant or expander would have to spend more on advertising to compete on a par [169]with the firm having the established brand. Gallo and United, with their firmly established brands, enjoy great advantages in this respect. They also have an advantage because of their large market shares. A firm attempting to enter or expand on a smaller scale than existing companies by spending an equal or greater amount on advertising will have a higher per unit cost because the total cost is applicable to a smaller number of units sold. It will be necessary, therefore, to make heavy advertising expenditures in order to achieve appreciable market penetration.

Consumer preference for certain brands has been "generated through extensive advertising and a long history of industry dominance." *General Foods,* 386 F.2d at 945. See *Procter & Gamble,* 63 F.T.C. at 1533; *Black and Decker,* 430 F. Supp. at 764. Wine is also a business in which brand name recognition and advertising capability have a definite impact on a firm's likelihood of success.

The use of advertising to create brand recognition (here in the wine industry) operates "as a formidable barrier to new market entrants who, in order to gain a significant foothold in the market, would have to withstand the powerful competitive weapons" presently employed by others which would "confront them upon their first entry." *General Foods Corporation,* 69 F.T.C. 380, 424 (1966). *Accord, Procter & Gamble,* 386 U.S. 568, 579 (1967) (recognition of advertising by others as a "major competitive weapon" confronting new entrant).

A product differentiation barrier exists when an entrant or expander must take affirmative steps to differentiate its product, whether through brand recognition or otherwise, in order to lure buyer loyalties away from similar products of an established seller or to capture the loyalties of new consumers. The Commission has observed that "[w]hether national advertising and distribution programs are viewed simply as a condition of entry . . . or as a means of creating substantial product differentiation, or a combination of the two . . . it is clear that these barriers" can be substantial. *Sterling Drug,* 80 F.T.C. 477, 597 n. 23 (1972).

The Commission has long recognized the product differentiation barrier. As explained in *The Procter & Gamble Co.,* 63 F.T.C. 1465, 1553 (1963):

> The term refers to consumer preferences as between very similar, close-substitute products or brands. Such preferences need not, and frequently do not, rest on real or substantial differences in terms of quality or usefulness. By reason of distinctive packaging, the firm's long history, mass advertising and sales promotions, or other factors, a firm may succeed in establishing such a definite [170]preference for its brand that the consumer will pay a premium to obtain it, although it is functionally identical to competing brands. Such brand allegiance, which the prospective entrant, marketing a new brand, will not, of course, command, may be the cumulative result of the expenditure of many millions of dollars over a period of many years to promote the brand, and may, in consequence, be very difficult to counteract even if the entrant makes a very substantial initial investment to promote his own brand. As a result, in an industry in which product differentiation is an important factor, not only may the new entrant find it especially difficult to pry customers loose from the established firms, but the higher price obtainable for a brand that has been successfully differentiated in the public mind from competing brands may impart a flexibility in pricing, akin to that imparted by cost advantages, which the newcomer may not be able to achieve for many years.

The record shows that the product differentiation barrier exists in the wine industry to such an extent that it constitutes a very substantial impediment to entry and expansion.

6. The Proliferation of Laws and Regulations Subsequent to Passage of the Twenty-First Amendment Constitutes an Additional Impediment to Competition in the Wine Industry

The Twenty-first Amendment, in addition to repealing Prohibition, also granted to the several states and territories the authority to regulate the sale and distribution of alcoholic beverages within their borders. The result has been a proliferation of varying laws and regulations among the states regarding such matters as wholesaling, label approval, price posting, markups, minimum prices, taxes and advertising.

It would appear that a company large enough to attempt a significant national entry or expansion in the wine industry would be able to hire the expertise necessary to cope with the various state statutes and regulations. Therefore, I do not consider this problem in itself to constitute a barrier to entry. Nevertheless, it is a situation which, when considered along with the various impediments and barriers discussed above, constitutes a real impediment to entry or expansion in the wine industry. [171]

7. New Entry Does Not Belie the Existence of Barriers to Entry

Many small new wineries have entered the industry (RX 1176). As interest in wine has increased in this country, many people have decided to try to make wine for themselves. In large part, these endeavors, which are required by law to operate as bonded wineries, are very small and may be characterized as "garage" or "one-man" operations (Tr. 7305; CX 192A). In terms of storage capacity, the new wineries account for a small percentage of industry growth and an even smaller percentage of total industry capacity (CX 459C–D).

The sheer number of new entrants means nothing when their total share of the market remains slight compared to the market leaders. *United States* v. *Black & Decker Manufacturing Co.,* 430 F. Supp. 729, 751 (D. Md. 1976); *Jim Walter Corp.,* 90 F.T.C. 671, 762 (1977). As in *Procter & Gamble,* 386 U.S. at 578, where the existence of some 200 fringe firms did not belie the fact that Clorox enjoyed a dominant position nationally, the existence of numerous, tiny new wineries does not belie the dominance of United and Gallo. This is true regardless of the age of such operations. In the wine industry, it is the leading firms that have captured by far the greatest share of growth (CX 458).

Nor do the number of new entrants belie the substantial barriers to entry or expansion characteristic of the relevant markets in this case. See *Black & Decker,* 430 F. Supp. at 751 and cases cited therein.

Barriers to significant entry or expansion exist wholly apart from what is required to start a household bonded winery.

Given an expanding market, such as wine, an increase in the number of competitors or even a rise of the sales of smaller firms at a faster rate is neither surprising nor inconsistent with an overall lessening of competition. *Jim Walter,* 90 F.T.C. at 762–63; *American General,* 89 F.T.C. 557, 636 (1972). New entrants may simply be prospering under the umbrella of weakened competition resulting from high levels of concentration in the market or responding in small part to rapidly increasing demand, without posing an immediate or certain threat to the leaders. *Ibid.*[49] In the wine industry we have the additional fact that many of the so-called "new entrants" are not even commercial operations but rather have been established as vocational pursuits.

More large-scale entry is expected to occur when demand is growing rapidly. Scherer, *Industrial Market Structure and Economic Performance* (1970) 229–30. Even to maintain its market position in a period of industry expansion, [172]a firm would have to grow. The leading firms would have to grow that much more to increase the concentration ratios. And that is what occurred in the all wine, dessert and sparkling wine markets from 1968–1972. As in *American General,* 89 F.T.C. at 640, the substantial increases in the four- and eight-firm concentration ratios from 1968 to 1972 show that the industry leaders "have made their gains primarily at the expense of the smaller members of the industry." The post-1972 data for the wine industry indicates that this has continued to be true, despite the rising demand.

Aside from the very small wineries of insignificant individual or aggregate volume, a few new entrants are plainly serious endeavors intent on establishing themselves with a place in the market on a noticeable, even if relatively small scale. Even these entrants, however, have had no effect on the concentrated state of the markets. Their record of success has been less than impressive. By expanding too quickly, some have sustained serious losses. See *American General,* 89 F.T.C. 557 at 637. To the extent that they still project success in the future, such projections, particularly in view of the difficulties others have experienced, should be greeted with some skepticism. *American General,* 89 F.T.C. at 637. Even if they meet their own projections, these firms would still be small in comparison to Gallo, United and other high ranking firms, and could easily take

[49] This is true even where, as here, the market share of a leading firm has dropped slightly. *Jim Walter,* 90 F.T.C. at 763.

their sales from the overall growth of the market without eroding the position of the market leaders.

VIII. ENTRENCHMENT OF UNITED'S DOMINANT POSITION

Entrenchment, as an antitrust violation, occurs when the acquiring firm affords additional competitive advantages to a dominant firm in a concentrated market. *Sterling Drug, Inc.*, 80 F.T.C. 477, 604 (1971). There, the Commission considered such factors as contributions to the acquired firm's production, distribution and marketing capabilities and resources *ibid.*; and, at 604 n. 29, the threat to change the structure of the industry and the effect of dissuading smaller firms from competing aggressively. The structure of the industry referred to by the Commission was that resulting from the raising of entry barriers, as recited in *FTC* v. *Procter & Gamble Co.*, 386 U.S. 568, 578 (1967).

In *Procter & Gamble, supra,* at 575, the Court discussed the heightening of such entry barriers as advertising costs, retail distribution and fear of retaliation by the industry leader. *Black and Decker,* 430 F. Supp. at 774 discussed " . . . the degree of synergy between the acquired and acquiring firms' marketing and manufacturing systems, between their technologies, and between their brand name recognition." *General Foods,* 386 F.2d at 945 noted the advantages in retail display and marketing which the acquiring company, "an even more formidable opponent," would enjoy. These elements are clearly present in this merger. [173]

It is not necessary that the acquired company's market share be increased. The maintenance or entrenchment of a large market share in a concentrated market is sufficient to constitute a violation.

United's market shares and market positions at the time of the merger were sufficiently large and significant in the all wine, table wine and dessert wine markets that it could be anticompetitively entrenched. In all wine, it had 17.9 percent of the market and its second place share was over six times that of The Taylor Wine Company which was in third position (Finding 498, *supra*). The entrenchment of such a share and such a market position clearly would be anticompetitive.

In table wine, United had 14.6 percent of the market and its second place share was 2.7 times that of Mogen David which, was in third position (Finding 499, *supra*). The entrenchment of such a share and such a position clearly would be anticompetitive.

In dessert wine, United had 21 percent of the market and its second place share was over six times that of The Taylor Wine

Company which was in third position (Finding 500, *supra*). The entrenchment of such a share and such a position clearly would be anticompetitive.

In sparkling wine, United was in third place with 10.7 percent of the market. As complaint counsel concede (CPF 1131), the entrenchment of such a share would not be anticompetitive in view of Taylor's 12.1 percent and Gallo's 11.3 percent market shares. Also, discounting Heublein (See discussion p. 112, and Finding 501, *supra*), the next two largest firms had 6.3 percent and 6 percent of the market, respectively. Thus, United was not in such a dominant position vis-a-vis the next smaller firms as it was in all wine, table wine and dessert wine.

The record establishes that the acquisition has served to entrench United's dominant market position in all wine, table wine and dessert wine.

The first barrier to entry discussed above was that of large capital requirements. Heublein, one of America's largest and most profitable corporations at the time of the merger, has financed United's operations with outstanding loans or lines of credit ranging at all times from $50 MM to $96 MM (Tr. 2515). This financing has been at rates lower than United could have secured elsewhere (Tr. 8121–25, 9473–76). Further, Heublein, which itself expends large sums for expansions in capacity (Findings 56–60, *supra*), announced almost immediately after the merger plans for a new United production facility for sparkling wine (Finding 61, *supra*). Also right after the merger, Heublein helped finance the $18 million dollar glass plant which has resulted in savings for United in the cost of glass and has operated at a profit. Heublein's participation in financing was to arrange [174]for $11 MM in bank loans by guaranteeing payments. It also was to contribute any additional operating capital that might be needed beyond that originally put up by United and Indian Head, the joint venturers (Findings 62–63, *supra*).

The merger has also entrenched United's ability to achieve distribution and, correspondingly, has increased that significant barrier to entry and expansion for others (Findings 590–652, *supra*). As one wine marketer testified:

> Every time there is an acquisition by a distiller of a winery or of a brand of wine, it makes it that much more difficult for a company like ours, an independent company to compete . . . (Tr. 1057).

At the time of the acquisition, Heublein had a large, well-established, nationwide distribution network for both wine and spirits. In most instances, its wines and spirits were distributed by

the same distributors (CX 93; Tr. 2464). As found above, Finding 258, *supra,* Heublein, as one of the inducements for Allied members to vote in favor of the merger, stressed the distribution advantages that would accrue to United by reason of Heublein's existing wide range of distribution of both spirits and wines. And the opportunity to take advantage of Heublein's distribution channels and selling muscle was one of the benefits of the then proposed merger recognized by Mr. Bruno Solari, President of United (Tr. 4967–68).

Heublein's past exercise of leverage with wholesalers to expand the distribution of Heublein products (Findings 645, 646, *supra*) shows both its capability and the likelihood of capitalizing on its importance to wine and spirits wholesalers to the distributional advantage of United and so increasing barriers to others.

The record otherwise demonstrates Heublein's intention to utilize the distribution advantages of the merger (See, *e.g.,* Finding 652, *supra*). While Heublein may have refrained to an extent, because of this suit, from generally exercising these advantages, Heublein currently has one common sales group handling national accounts such as airlines, chain hotels and chain restaurants for both its spirits products and United's products (Finding 135, *supra*).

Heublein's ability to maintain and protect United's shelf position through advertising (and other non-price marketing tools) and through use of secondary lines of wines may result in a raised barrier at the retail shelf level (Findings 670–74, *supra*). And the likelihood of United securing greater shelf space was one of the advantages of the proposed merger recounted to Allied's members by the spokesmen for Heublein (Finding 665, *supra*). [175]

Clearly, the merger will significantly increase the advertising and brand recognition or product differentiation barrier. The acquisition of United by Heublein, one of the leading marketers and advertisers in the nation, provides the capability of significantly increasing advertising and merchandising efforts in support of United's already well-established brands. And by May 1970, United's wines were supported by what was then probably the most intensive and extensive advertising campaign of wine promotion ever undertaken by a single company in this country (Finding 729, *supra*).

Heublein is a very strong marketer and merchandiser (Findings 118–148, *supra*). In 1965, it asserted that it had a "reputation in the industry as perhaps the most astute and successful merchandisers of alcoholic beverages" (CX 178A).

Its outstanding, indeed spectacular, successes with Smirnoff Vodka (Findings 27–32, 47, 49), Harveys Bristol Cream (Findings 34–35, 45, 133), Lancers (Findings 37, 38, 46, 49, 133), Heublein Cocktails

(Finding 33), Arrow Cordials and Brandies (Findings 36, 46, 49) and Jose Cuervo and Matador Tequila (Findings 39, 49) demonstrate its capabilities. The superimposition of these capabilities upon United can only serve to entrench United's dominant position.

Conclusion

I find that Heublein's acquisition of United entrenched United's dominant position and strengthened barriers to significant entry or expansion in the all wine market and in the table and dessert wine submarkets.

IX. POTENTIAL EXPANSION

A. Heublein Was an Actual Potential Expander into the Domestic Segment of the United States Wine Industry

784. As of the time of its acquisition of United, Heublein was an actual potential expander in the United States wine industry by entry into the domestic segment of the industry; and, but for the acquisition of United, would have entered by alternative, more procompetitive means. The record shows, by both objective and subjective evidence, that Heublein definitely intended to expand its position in the market by entering the domestic segment, had explored various means of so doing, and was capable of expansion *de novo* or by toehold acquisition.

785. Heublein had not only the capability, but also the incentive to expand its position in the wine industry by entering the domestic segment. Heublein was an aggressive growth company (Tr. 4438). The wine industry was experiencing a period of rapid growth and appeared attractive (Tr. 4456–57, 5117). Heublein had a high return on capital, was seeking [176]additional high return opportunities and the wine industry offered such an opportunity (Tr. 5117). Heublein could put to use in related fields the marketing and advertising skills which it possessed (RX 1215; Tr. 4439). Heublein could put to use its familiarity and capability with respect to supermarket and alcoholic beverage channels of distribution (Tr. 4945–46).

1. Heublein Was a Small but Important and Growing Force in the United States Wine Industry

786. At the time of the acquisition, Heublein's market share in the all wine, dessert wine and table wine markets was relatively small. Nevertheless, because of the concentrated state of the market,

it ranked sixteenth, thirteenth and thirtieth in those markets, respectively. Until Heublein, by its own choice after the merger, repositioned Lancers from a sparkling wine, it ranked fourth in the sparkling wine submarket.

787. Heublein had been in the wine business only since 1957, but since that time it had experienced a very rapid growth. From 1963 to 1968, sales of its two leading wines had increased—84 percent for Harveys Bristol Cream Sherry and 294 percent for Lancers. In the fiscal year in which the acquisition occurred, sales of both products increased again (Findings 45, 49, *supra*).

788. As the market share tables for 1967 and 1968 show, Heublein's wine business was growing fast enough to improve its market position and, in the all wine and table wine markets, to move up in rank:

	1967	*1968*
Heublein	*Market Share (Rank)*	*Market Share (Rank)*
All wine	.63% (17)	.79% (16)
Dessert wine	.45% (13)	.54% (13)
Table wine	.20% (31)	.23% (30)
Sparkling wine	6.0 % (4)	7.2 % (4) (CX 373)

789. Heublein prided itself as a growth company and actively pursued a growth and diversification policy. Included in this was an active determination to expand its position in the fast growing wine industry, particularly the domestic segment. The only realistic assessment of Heublein's market position but for the merger is that it would have continued to grow at an impressive rate.

790. In 1967, Heublein reported that the wine portion of its business had grown rapidly and accounted for an important share of total sales and earnings. In acknowledgement of this growth, Heublein expanded the sales force covering its wine market and gave its top brands special attention (CX 48K). [177]

791. In 1968, Heublein's Annual Report reflected awareness of the substantially increasing consumption of wines and increased consumer interest in wines (CX 49K). It reported that the trend toward flavorful, light alcoholic drinks was a factor contributing to the growth of wine sales (CX 49M).

792. In October 1968, Heublein told its stockholders that its "success with imported wines has accentuated our interest in domestic wines" (CX 34G). It showed its further awareness of the

opportunities in wine by saying, "We believe that California wines are about to enter an era of rapid growth" (CX 34G).[50]

793. Heublein had expertise in the wine business (CX 37B), having achieved its initial market share in wine with only two major single-item products (CX 320, 373D, N, Y, Z–9).

2. Heublein Was a Major Industrial Corporation, a Leading Marketer of Alcoholic Beverages

794. At the time of the acquisition, Heublein was the largest wine importer in the United States and in the year following the acquisition was the fifth largest domestic producer of alcoholic beverages (Finding 15, *supra*). In the year of the acquisition, Heublein distributed 22 brands of spirits, ten of which it produced (Finding 22, *supra*). In the year of the acquisition, Heublein distributed 24 primary brands of wine (excluding United and Beaulieu) and others in limited quantities (Findings 23, 24, *supra*). In addition, Heublein produced three brands of beer and malt liquor (Finding 25, *supra*) as well as specialty foods (Finding 26, *supra*). Heublein's legendary success with Smirnoff Vodka, Lancers Rose and Harveys Bristol Cream Sherry has been discussed above (Findings 27–32, 34–35, 37–38), as has its success with canned cocktails, tequila, rum, and the Arrow line of cordials and brandies (Findings 33, 39, 71).

795. One of the reasons for Heublein's great success and growth over the years was its strength in marketing. Aggressive, effective marketing was a major point of pride with Heublein. Heublein originated prepared cocktails and with its Smirnoff vodka it pioneered the rapid growth of the vodka market, leading it from virtually nothing to become one of the major distilled spirits categories. Even when Heublein was not setting the trends, it was keeping pace with them. For example, as interest in travel increased, Heublein took the [178]lead in marketing distilled spirits to the airlines and to other travel accounts (Finding 127, *supra*).

796. Heublein was a leading producer and importer of the distilled liquors commonly known as "white" goods, notably vodka, gin, rum and tequila. Indeed, in 1968, Heublein considered itself to be "in a unique position with representative brands in all eight of the fastest growing categories of distilled spirits" (CX 49K). Heublein was capitalizing on the trend toward the light taste in alcoholic beverages with its spirits products and its wines.

797. Heublein regularly introduced and promoted new products,

[50] While these statements were made after entry into the merger agreement, they reflect the prior existence of an overall interest in domestic wines not limited to the particular merger.

and it emphasized the full range of marketing activities including merchandising and packaging. It was a major advertiser and used its advertising effectively to promote sales.

798. Heublein had a well-established and strong distribution network. At the time of the acquisition, it was the fifth largest distilled spirits supplier in the country. Today it is number two. Several of its products, including its Lancers and Harveys Bristol Cream wines, were "call" or "demand" items in retail accounts. As a result of this, in addition to its size, Heublein's strength in terms of wine and spirits distribution gave it a very real advantage and incentive in expanding its market position further. In addition, Heublein had demonstrated knowledge and capability with respect to distribution through supermarkets, where a growing percentage of wine sales were occurring.

799. Heublein sells to distributors, state agencies, transportation and military accounts (CX 4, 16, 56Z–7).

800. Heublein is in a dominant position vis-a-vis its distributors and is able to secure distribution advantages (pp. 218–240).

801. There were approximately 400 Heublein spirits distributors in 1972 (Tr. 8797).

802. Heublein was interested in acquiring products that could be sold through its spirits distribution channels (Tr. 3929).

803. When Heublein obtained the rights to sell Harveys, it increased Harveys distribution by placing it with Heublein wholesalers (Tr. 3985–86).

804. Prior to the acquisition of Vintage Wines, Inc., Heublein's imported wines were marketed through the Smirnoff Beverage and Import Co. (Tr. 8651). When Heublein acquired Lancers, it was placed in the Heublein spirits division (Tr. 8658). [179]

805. Heublein believed that Lancers wine "lends itself to our type of distribution" (CX 46G).

806. Lancers and Harveys wines were sold in part through distributors that handled Heublein spirits products (Tr. 3924).

807. The Heublein spirits sales force handles Beaulieu Vineyard Wines (Tr. 9841).

808. Heublein believed that United's wine products were compatible with its own. Heublein told Allied's members this compatibility could be beneficial in the distribution of United's products, because Heublein could place United products with its distributors, and mentioned Smirnoff as a primary example of one of its compatible products (Tr. 2464–68).

809. Heublein representatives stated that by having domestic wine to go along with Smirnoff, Lancers and other Heublein

products, United's distribution system would be greatly enhanced by using Heublein's warehouses and distributors and, similarly, Heublein would be able to use United warehouses and distributors. This would result in greater overall distribution (Tr. 2691).

810. Mr. Carriuolo, Heublein's Executive Vice President, believed that an alliance with Heublein would give a small winery an advantage in terms of distribution as well as in other ways (CX 208B).

3. Heublein's Efforts To Implement Its Corporate Growth and Diversification Policy Pointed toward Expansion in Wine

811. Heublein was a "growth" company with strong financial resources as measured by its excellent price earnings multiple for its shares, by its ability to generate internal funds from profits, and by its access to external funds at favorable rates. Heublein's growth was achieved by acquisition of established businesses, new products and lines, expansions in capacity, and by marketing new brands (by acquisition and distribution agreements) of products already being marketed by Heublein. In deciding upon candidates for acquisition, Heublein looked for products compatible with its marketing skills and channels of distribution (*e.g.,* supermarkets or spirits distribution channels), and which would expand the kinds of businesses it was already in (Finding 91, *supra*).

812. In the early 1960's, one Ray Weiser, who identified himself as representing Heublein's importing company, told Louis Gomberg, a wine property broker, that Heublein was [180]interested in the Alta Vineyards Company[51] (Tr. 1415). At the time Schenley sold Alta Vineyards in 1963, it was substantial in size and had an established distribution network (Tr. 2971–73).

813. In January 1965, Ed Kelley, Vice President of Heublein, advised a merger consulting firm that Heublein would not be interested in acquiring a wine distributor unless it owned all or a substantial portion of its brands and the brands were other than "price" items, in which case it might be interested and would appreciate further information (CX 173–74).

814. In 1965, John Martin, Heublein's Chairman, wrote to a financial representative to express Heublein's interest in acquiring

[51] HUV would dispute this finding on the ground that "There is absolutely no proof that Mr. Weiser was even employed by Heublein, or what position, if any, he held with any company" (RRPF 337). However, there is no reason to reject the particulars of the contact between Mr. Weiser and Mr. Gomberg as related by Mr. Gomberg, and Mr. Gomberg could not reasonably have been expected to verify the fact and nature of Mr. Weiser's employment by Heublein. Heublein was in a position to present any evidence to refute the related fact that Mr. Weiser was employed by Heublein. Heublein having failed to offer any such evidence, I have accepted the testimony of Mr. Gomberg.

the Taylor Wine Company. Mr. Martin indicated that he had already had an exploratory talk on the subject with Taylor people and, although Taylor was not presently interested, he wanted a follow-up on the matter (CX 165). Various reports on Taylor to Heublein followed (CX 166-69), although nothing ever came of the matter.

815. Mr. Kelley, Heublein's Vice President, said that the Taylor Wine Company was one of the alternative acquisition candidates for Heublein and that they studied it as thoroughly as one could without having inside information (Tr. 4542).

816. Heublein, as early as mid-1965, had contacts with representatives of Almaden and advised them of Heublein's interest in acquiring that company (CX 139–42).

817. In January 1967, after having been advised that Almaden was willing to sell, Heublein prepared an outline of a proposal to purchase and made an offer of purchase. The offer was approximately $12 million (Tr. 917; CX 144–47).

818. On or about August 17, 1967, the Charles Krug Winery was suggested to Heublein as an acquisition possibility. The information was immediately passed on to Mr. Edward Kelley, Heublein's Executive Vice President, who was then responsible for long-range planning (CX 148; Tr. 4425–26). As of October 2, 1967, the matter was still under consideration (CX 152). [181]

819. In December 1967, Ed Kelley, Heublein's Executive Vice President, informed a broker for the Mogen David Wine Company that he would "think about" that winery but that Heublein was then "considering other wine possibilities" (CX 197). Mr. Watson, Heublein's Chief Executive Officer, suggested that Mr. Martin, the Chairman, should make any initial contact because of his "direct access to Mogen-David" (CX 198). After reviewing the matter, Heublein decided not to pursue the acquisition of Mogen David (CX 203).

820. In March 1968, Chris Carriuolo, Heublein's Senior Vice President, reported to Heublein's Executive Vice President that he had had a discussion with Lee Knowles, Vice President of Beaulieu Vineyards (CX 207). Mr. Carriuolo stated that "because of our [Heublein's] interest in the U.S. wine business," Heublein should consider several kinds of agreements with Beaulieu in order to get closer to the company with the view of eventually taking it over (CX 207B). He expressed his understanding that Heublein's Mr. Martin and Mr. Hart had approached Beaulieu about the possibility of buying it a few years before (CX 207A). Nearly a year later, Mr. Carriuolo reported his further efforts to develop ties with Beaulieu

(CX 208B), and, on June 5, 1969, the company was acquired by Heublein (Finding 78, *supra*).

821. In the Spring of 1968, Heublein executives had focused on wine as an area of expansion opportunity (Finding 92). Previously, Heublein had explored the possibilities of foreign production of wine (Tr. 346, 4732); and, as far back as 1966, Heublein's long-range planning group had identified wine as a product suitable for diversification. In March 1968, Heublein's Executive Vice President referred to " . . . our interest in the U.S. wine business" (CX 207B). At that time, Heublein was not interested in "small vintage wine types" of wine companies (Tr. 4950), but was interested primarily in a California winery (Tr. 4955).

822. In the early summer and fall of 1968, Heublein considered the acquisition of the San Martin Winery (CX 185–90). Heublein's Mr. Beckstoffer visited San Martin, collected information about the winery, discussed the various arrangements that could be made and reported back to Heublein's Executive Vice President (CX 187). Heublein obtained a detailed report on various aspects of San Martin from wine industry consultant Louis Gomberg (CX 188).

823. At Heublein's request (CX 191A), wine industry consultant Louis Gomberg, in the fall of 1968, submitted reports to it regarding several domestic wineries that might be acquisition candidates (CX 191). [182]

824. Also at Heublein's request, Mr. Gomberg reviewed a number of wineries that Heublein might use "in bridging the price gap between the top of the Italian Swiss Colony line and the bottom of the Inglenook line" (CX 192A). In reviewing the field of candidates, Mr. Gomberg reported on the prospects of acquiring each winery (CX 192E, F) and, if the winery were small, on expanding it (CX 192G).

825. During the period of discussions with United, Heublein did not reject, but merely postponed merger talks with Guild, a small winery, pending completion of "a study of the alternatives of how to enter the wine industry" and of its negotiations with United (Tr. 4512–13).

826. When Mr. Ed Kelley, Executive Vice President of Heublein was placed in charge of planning in March 1968, one of Heublein's corporate objectives was to enter the wine industry within one to three years. And this goal was assigned to Mr. Kelley (Tr. 9279–86).

827. Subsequent to the acquisition, Heublein reported to its stockholders in the 1969 Annual Report that "The addition of the

domestic wine business to an already flourishing imported wine business was one of our three corporate goals"[52] (CX 50E).

828. I conclude that Heublein had the intent and capability to expand into the domestic wine industry at the time of its acquisition of United;[53] and, but for the acquisition would have entered by other means in the near future. In light of Heublein's proven capabilities and successes, particularly in the imported segment of the wine industry, it may also be anticipated that its expansion into the domestic segment of the wine industry would have had a significant competitive impact. [183]

B. The Merger Violated Section 7 of the Clayton Act under the Actual Potential Entrant (Expander) Doctrine

Heublein's acquisition of United, a dominant firm in the concentrated United States wine industry, had the anticompetitive effect of eliminating Heublein as an actual potential competitor. Section 7 of the Clayton Act "looks not merely to the actual present effect of a merger but instead to its effect upon future competition." *United States* v. *Von's Grocery Co.,* 384 U.S. 270, 277 (1966). A merger's effect upon future (potential) competition may be either the edge effect (the "waiting-in-the-wings" or "on the fringe" perceived potential competitor effect), or the entry (actual potential entrant) effect.

The court in *United States* v. *Phillips Petroleum Company,* 367 F.Supp. 1226 (C.D. Cal. 1973), *aff'd,* 418 U.S. 906 (1974), discussed the theoretical foundations of the actual potential entrant doctrine as follows:

> The crux of the entry effect is that if the company which enters the market by acquisition had entered unilaterally,[4] it could have supplied an additional competitive force without eliminating one already present in the market. An acquisition of a company in the market by a company which is likely to enter on its own thus has an anticompetitive effect on the market.

[4] . . . the terms 'unilateral entry', 'independent entry', or '*de novo* entry', . . . denote entry into a market through the entering firm's own efforts without a purchase or acquisition of stock or assets of a firm already in the market other than of a *de minimis* nature (at 1232).

[52] The other two objectives "were record growth in sales and earnings-per-share and the successful introduction of profitable new products" (CX 50E).

[53] As developed above, the barriers and impediments to entering the wine market would not have been substantial barriers to Heublein. Heublein had, or had ready access to, the necessary capital; its compatible distribution system was already in operation and it had the influence with wholesalers to secure additional wine distribution as required; it was in position to obtain the necessary retail shelf space; it was a national leader in advertising and promoting products to develop brand recognition and preference; and it was fully acquainted and capable of coping with the multitude of varying state laws and regulations.

In *United States* v. *Black and Decker Mfg. Co.*, 430 F. Supp. 729 (D. Md. 1976), the court reviewed the case development of the actual potential entrant doctrine,[54] and summarized the analytical prerequisites enunciated therein as follows: [184]

> In a nutshell, review of prior potential competition cases suggests that the competitiveness of the market first be determined; the feasibility of alternative means of entry to a leading firm acquisition must then be explored with reference to the incentive and capability of the acquiring company; and finally, the ability of those alternative means of entry, if any, to deconcentrate or provide significant procompetitive effects must be examined (at 748).

Applying those criteria to the facts of this case, it is clear that Heublein was an actual potential competitor whose elimination had an anticompetitive effect. First, as discussed above, at the time of the acquisition concentration ratios in the relevant market (all wines) and in the three submarkets was high. Furthermore, market shares in the all wine market and in the table and dessert wine submarkets were skewed by the high shares of only two dominant firms, one of which was United.

Second, Heublein had feasible alternative means of entry in terms of its incentive and capability. As noted above, Heublein intended to expand in the domestic wine industry because such products would allow it to efficiently utilize its marketing experience and ability and its distribution channels for imported wines and domestic and imported spirits. Heublein's incentive and ability to expand in the wine industry distinguish this case from such conglomerate mergers as *Missouri Portland Cement Co.* v. *Cargill, Inc.*, 498 F.2d 851 (2nd Cir.), *cert. denied*, 419 U.S. 883 (1974); and *Federal Trade Commission* v. *Atlantic Richfield Company*, 549 F.2d 829 (4th Cir. 1977). In the latter, the Commission challenged the acquisition by Arco (a producer of petroleum, natural gas, and uranium) of Anaconda Co. (a miner and producer of copper and aluminum). There, in an action brought by the Commission for preliminary injunction to prevent consummation of the merger during pendancy of administrative antitrust proceedings, the court found that the Commission had failed to show substantial likelihood of success in demonstrating the anticompetitive effect of the merger:

> . . . the conglomerate merger in the instant case involves no product or market extension; it is a merger purely for purposes of diversification. Arco is not poised on the fringe of the copper markets; it has no technological skills readily transferrable to

[54] *United States* v. *Marine Bancorporation*, 418 U.S. 602 (1974); *Federal Trade Commission* v. *Procter & Gamble Co.*, 386 U.S. 568 (1967); *United States* v. *Falstaff Brewing Corp.*, 410 U.S. 526 (1973); and, *United States* v. *Phillips Petroleum Company, supra.*

the copper markets; it has no channels of distribution which may be utilized to distribute copper (at 295). [185]

Heublein's acquisition of United was a product extension merger into the domestic wine business for which it had readily available the technological marketing skills and distribution channels such as were noted in *Federal Trade Commission* v. *Procter & Gamble,* 386 U.S. 568, 580 (1967), and *Federal Trade Commission* v. *General Foods,* 386 F.2d 936, 945 (3rd Cir. 1967).

Heublein's intent to expand in the United States wine market was formulated and accomplished within a definite time frame: one to three years from the time its executives were assigned the goal of expansion in this industry (Finding 826, *supra*). The facts of this case thus meet the " . . . reasonable temporal estimate related to the near future," requirement announced in *BOC International Ltd.* v. *Federal Trade Commission,* 557 F.2d 24, 29 (2nd Cir. 1977).

Heublein had the financial capability for either *de novo* or toehold entry. It had for several years been exploring the possibilities of acquiring specific small wineries and had made efforts toward that end (Findings 812–25, *supra*). Indeed, it had acquired Beaulieu in a move that culminated efforts that preceded, and were totally unrelated to, the acquisition of United (Findings 78, 820, *supra*). Heublein could have made such an acquisition or acquisitions and expanded production in the manner pursued by Almaden and indeed as it did with Inglenook in developing their "Mountain" and "Navalle" lines, respectively, or in the manner of its extension of the Lancers line from rose into Vinho Branco white wine and Rubeo red wine (Findings 65, 106–10, 203, 204, 315, 688, 690, 691, 713, *supra*). At the time of the acquisition, Heublein was financially strong, capable of financing its investments in new products through internally-generated profits, by borrowing from external sources at favorable rates or by purchase with shares of Heublein stock, which was the method used to purchase United. It was also able to provide financial support to its acquisitions and new endeavors, *e.g.,* the $96 million credit extended to United after the acquisition (p. 173, *supra*). Heublein's expansion in the United States wine industry was financially feasible.

Heublein's expansion in the United States wine industry *de novo* or by toehold acquisition and subsequent expansion in the manner of Almaden and Inglenook would have had procompetitive consequences. A major advertiser and strong marketer would have been introduced into the market to challenge the dominance of Gallo and United.

I therefore conclude that Heublein was an actual potential

expander in the United States wine industry in 1968 with the incentive and capability of expansion within one to three years, and on a sufficiently large scale to challenge the dominance of Gallo and United. [186]

X. CONCLUSION: THE PROBABLE EFFECT OF HEUBLEIN'S ACQUISITION OF UNITED VINTNERS MAY BE TO SUBSTANTIALLY LESSEN COMPETITION IN THE UNITED STATES WINE INDUSTRY

Prior to the merger, Heublein's shares of the relevant markets were:

all wine .79 percent (16th in rank)
table wine .23 percent (30th in rank)
dessert wine .54 percent (13th in rank)[55]

These percentages are superficially small, although not appreciably smaller than the 1.3 percent and 1 percent held to be anticompetitive increments to a dominant firm's share in a concentrated market in *United States* v. *Aluminum Company of America,* 377 U.S. 271 (1964) and *Stanley Works* v. *FTC,* 469 F.2d 498 (2nd Cir. 1972), *cert. denied,* 412 U.S. 928 (1973), respectively.

In *United States* v. *General Dynamics Corp.,* 415 U.S. 486 (1974), the Court discussed the role of market share data in antitrust analysis:

> In most situations, of course, the unstated assumption is that a company that has maintained a certain share of a market in the recent past will be in a position to do so in the immediate future. Thus, companies that have controlled sufficiently large shares of a concentrated market are barred from merger by Sec. 7, not because of their past acts, but because their past performances imply an ability to continue to dominate with at least equal vigor. In markets involving groceries or beer, as in *Von's Grocery, supra,* and *Pabst, supra,* statistics involving annual sales naturally indicate the power of each company to compete in the future. Evidence of the amount of annual sales is relevant as a prediction of future competitive strength, since in most markets distribution systems and brand recognition are such significant factors that one may reasonably suppose that a company which has attracted a given number of sales will retain that competitive strength (at 501). [187]

The most basic premise of the antitrust laws, that increasing concentration leads to anticompetitive interfirm coordination, requires that any significant increment in the share of a dominant firm in a concentrated industry be prevented. The Court held in *United States* v. *Philadelphia National Bank,* 374 U.S. 321 (1963)

[55] Heublein's share of the sparkling wine submarket is not being considered here for the reason stated at p. 112, *supra.*

that " . . . if concentration is already great, the importance of preventing even slight increases in concentration and so preserving the possibility of eventual deconcentration is correspondingly great" (at 365 n. 42). And in *United States* v. *Aluminum Co. of America,* 377 U.S. 271 (1964), the Court noted that the objective of the 1950 amendments to Section 7 of the Clayton Act "was to prevent accretions of power which 'are individually so minute as to make it difficult to use the Sherman Act test against them' " (at 280).

Therefore, the evaluation of whether Heublein's small shares of the all wine market and of the table and dessert wine submarkets were *de minimis* as of the time of the merger must be made in light of the recognition in *Philadelphia National Bank* and *Aluminum Co. of America* that "slight" or "minute" accretions in concentration or power must be considered under Section 7. Further, as of the time of the merger, Heublein's shares of the markets were growing. Its percentage shares, therefore, understate the probability of the potential future increment. In addition, Heublein's distribution rights to Harveys and Lancers, items of great prestige and consumer demand, were more significant than their small shares of the industry would indicate.

Under the circumstances recited above, the potential market share increment to United's already dominant position is found not to be *de minimis* and the acquisition violates Section 7.

As previously found, Heublein has also violated Section 7 by reason of its entrenchment of United's dominant position (pp. 172–75, *supra*), as well as by elimination of Heublein as an actual potential competitor (pp. 183–85, *supra*).

Therefore, Heublein has violated Section 7 under the three separate principles enunciated above. Under a broader view, Heublein has violated Section 7 because of the totality of these three anticompetitive effects (the increased concentration, the entrenchment of United, and the loss of Heublein as a significant actual potential competitor). The anticompetitive effect of all three elements considered together is, of course, greater than that of any one evaluated separately.

Heublein and United have asserted as an affirmative defense that "But for Heublein's acquisition of a controlling interest in United, United's predecessor cooperative associa[188]tion was destined to remain an ineffective competitor." In their post hearing submittal, HUV argue that at the time of the merger, United was clearly in a weakened financial and competitive position and did not have the ability to maintain into the 1970's the position it had enjoyed in the early to mid-1960's (RPF 102).

To the contrary, the record shows that United was the second largest company in the relevant markets (except for sparkling wine where it ranked third) at the time of the merger with market shares significantly larger than the third largest company. It also shows United's ability to maintain its position in the table wine market as consumer demand shifted from dessert to table wines. When a new opportunity arose in the wine industry, refreshment wines, United had the ability to secure almost 40 percent of that market, outselling the number three competitor many times over.

The findings descriptive of United prior to the merger (150–86, 190, 209–18, 222–41) depict a successful and aggressive company with multiple plants producing all types of wines and selling its products through 370 distributors and its own distribution system, in all 50 states and the District of Columbia.

It had acquired the Italian Swiss Colony line, among others, from Petri in 1957 for $24 million and had repaid that purchase price a year and a half ahead of schedule. United had also acquired the prestigious Inglenook Winery in 1964.

United was a leading advertiser in the wine industry and its president and chief executive officer was considered one of the most astute merchandisers in the wine business. United was consistently profitable, a financially strong company.

As of the time of the merger, United was planning a new table wine brand and had taken steps toward constructing a $10 million glass plant. United had been able to borrow money at reasonable interest rates as required.

Allied's membership increased from 230 grape growers in 1951 to over 1,600 in 1968, and members were anxious to participate in the cooperative venture. There was a waiting list of 100,000 tons of grapes the growers wanted to deliver through Allied.

HUV's discussion (RPF 53–102) of United's and Allied's operations is claimed to demonstrate a defense within the holding of *United States* v. *General Dynamics,* 415 U.S. 486 (1974). There, the Court found that statistics showing the acquired company's market share did not reflect its ability to compete because the company lacked uncommitted reserves [189]of coal and could not acquire any with which compete for future business. In this case, to the contrary, United (through Allied) was able to secure the raw material it required. There was no basic impediment to the continuation of United's vigorous competitive position.

The facts relied upon by HUV, interpreted in their very worst light, reflect business and organizational problems soluble in the normal course of operations. HUV's assertions that these present

problems which presage a diminution of United's competitive position are too conjectural for adjudicative determination. The record does not indicate that United could not have resolved its alleged difficulties. HUV's assertions are insufficient to comprise a "failing company" defense.[56]

XI. REMEDY

A. Divestiture of United Vintners

The principal purpose of relief in a Section 7 case is to restore competition to the state in which it existed prior to, and would have continued to exist but for, the illegal merger. . . . Ordinarily, a presumption should favor total divestiture of the acquired assets as the best means of accomplishing this result, *United States* v. *Continental Can Company, Inc.*, 1964 ¶ 71,264 at p. 80,183 (S.D.N.Y. 1964) . . . ., *RSR Corp.*, 88 F.T.C. 800, 893 (1976).

Divestiture in this case is both necessary and appropriate to remedy the anticompetitive effects of the acquisition. The Heublein share of the market will be removed from United. United will be restored to its former competitive position, a positive benefit for the market since United will no longer be bolstered by the entrenching effects of Heublein's resources. And Heublein will be repositioned as an actual potential competitor.

HUV have argued that, in the event of an order of divestiture, it should not be required to divest Jacare, Esprit and T.J. Swann, trade names owned by Heublein and which came into existence after the acquisition (RR 352). The inclusion of after acquired proprietary rights to T.J. Swann and Esprit in the order of divestiture is necessary and appropriate to maintain United's competitive integrity. At the time of the merger, United already had a strong share of the refreshment wine market while Heublein marketed no such wines (Finding 513, *supra*). [190]

T.J. Swann, thereafter, was produced and distributed by United as a continuation of its endeavors in the refreshment wine market. It is a high volume, profitable brand (Finding 195, *supra*) and it must be divested with United. Esprit is another refreshment wine developed by United (Tr. 9544-45), and thus should not be excluded from the divestiture. Jacare originally was the name of a Lancers type carbonated wine developed by Heublein in the facility partially owned by Heublein in Portugal. The wine was test marketed in the United States but was a failure and was discontinued before United was acquired by Heublein. The Jacare wine being sold by United

[56] As previously found (Finding 262, *supra*), United was not sold because of an inability to continue in business on its own, but rather in response to what appeared to be an advantageous offer which was initiated by Heublein.

today is a California wine developed and produced by United. It is a table wine and has no resemblance to the product previously sold by Heublein under the Jacare label (Tr. 321–27, 4438, 4486, 9977–78). Jacare, therefore, is not being excluded from divestiture.

Divestiture of T.J. Swann, Esprit and Jacare is being ordered because these products are an integral part of the United product line. Divestiture does not depend upon Heublein's choice as to which company holds title to the trade names under which United does business.

Complaint counsel would have Heublein prohibited, for ten years, from acquiring, without Commission approval, any interest in any concern engaged in the production, importation, distribution and/or sale of wine. Such a sweeping prohibition would be inconsistent with the actual potential entrant basis of this case. One of the reasons Heublein's acquisition of United violated Section 7 is because it removed Heublein as an actual potential entrant. The order of divestiture is procompetitive, in part, because it repositions Heublein as an actual potential competitor, allowing potential entry by toehold acquisition. The provision requested by complaint counsel would preclude this procompetitive element of the order. In addition, as proposed, the provision would prohibit vertical integration to facilitate distribution. This case involves a horizontal acquisition with product extension and entrenchment aspects. There is no basis for prohibiting vertical integration.

In *Budd Company,* 86 F.T.C. 518, 582 (1975), the Commission announced a general presumption that a firm holding 10 percent or less of a target market would be considered a "toehold" firm. Consistent with that principle, the prohibition against further acquisitions is being limited to situations where the acquisition or acquisitions would increase Heublein's total share of the relevant market or submarkets to over 10 percent. Such a provision would permit toehold acquisitions in the markets as they exist today and would allow for considerable market change before a toehold acquisition might be prohibited. Heublein may seek Commission [191]approval of an acquisition which would be inconsistent with the 10 percent limitation or, upon a showing of changed conditions of fact or as a matter of public interest, may seek such modification as may be appropriate under Section 3.72(b) of the Rules of Practice.

B. Dismissal of the Complaint Against Allied Grape Growers, United Vintners, Inc., and Heublein Allied Vintners, Inc.

Under the terms of the acquisition, United was converted from an agricultural cooperative association into a corporation which then

became a wholly-owned subsidiary of Heublein Allied Vintners. Heublein Allied Vintners was owned by Heublein (82 percent) and Allied (18 percent). On September 13, 1978, Allied moved for its dismissal from the proceeding upon a showing that it had sold its 18 percent interest in Heublein Allied Vintners to Heublein which then owned 100 percent of Heublein Allied Vintners and, through it, 100 percent of United. Allied also abandoned all claims formerly made in this case including the right of first refusal in the event Heublein should be required to divest itself of its interest in United. On November 9, 1978, Heublein Allied Vintners merged into Heublein and ceased to exist. Heublein thus now owns directly 100 percent of United (pp. 7–9, *supra*).

Relying upon the foregoing, Heublein United Vintners and United, on December 13, 1978, also moved for dismissal of the complaint against them. I deferred ruling on all three motions for dismissal until the initial decision. In their post-trial memorandum (CB 3), complaint counsel state that they do not oppose any of the three motions.

In consideration of the order being issued against Heublein which affords all of the relief required in this case, any order issued against Allied Grape Growers, United Vintners, Inc. or Heublein Allied Vintners, Inc. would be superfluous. Therefore, I am dismissing the complaint as to these three respondents.

Order

I

It is ordered, That the complaint against Allied Grape Growers, Heublein Allied Vintners, Inc., and United Vintners, Inc. be, and it hereby is, dismissed.

II

It is further ordered, That, subject to the prior approval of the Federal Trade Commission, respondent Heublein, Inc. (hereinafter "Heublein"), a corporation, its successors and assigns, and its officers, directors, agents, representatives, [192]employees, subsidiaries and affiliates, shall, within one year from the effective date of this Order, divest all of the stock of United Vintners, Inc. and all assets, rights, property and privileges, tangible and intangible, including all plants, equipment, machinery, raw material reserves, inventory, customer lists, trade names, trademarks, good will and other property, including all additions and improvements thereto, of

whatever description acquired by Heublein as a result of its acquisition of any interest in Heublein Allied Vintners, Inc. and, thereby of its wholly-owned subsidiary United Vintners, Inc. (hereinafter "United"), formerly a wholly-owned subsidiary of Allied Grape Growers (hereinafter "Allied"), or acquired by Heublein as a result of the sale to Heublein by Allied of Allied's interest in Heublein Allied Vintners, Inc. or the subsequent merger of Heublein Allied Vintners, Inc. into Heublein, and all trade names under which wine is produced and marketed by United, including but not limited to Jacare, Esprit and T.J. Swann.

III

It is further ordered, That for a period of ten (10) years from the date of approval of the divestiture required by this Order, Heublein shall not acquire, directly or through any corporation, subsidiary, division or other device, without the prior approval of the Federal Trade Commission, the whole or any part of the stock, share capital, assets or any other interest of or in any concern engaged in the production, importation, distribution and/or sale of wine, where Heublein's and said concern's combined share of the United States all wine, table wine, dessert wine or sparkling wine market or submarket would exceed 10 percent; nor shall Heublein enter into any arrangement with any concern by which Heublein obtains the market share in whole or in part, of any concern involved in the production, importation, distribution and/or sale of wine whereby Heublein would possess a total share in excess of 10 percent of the United States all wine, table wine, dessert wine or sparkling wine market or submarket.

IV

It is further ordered, That pending divestiture, Heublein shall not make or permit any deterioration in the value of any of the plants, machinery, parts, equipment, or other property or assets to be divested that may impair their present capacity or market value unless such capacity or value is restored prior to divestiture, nor shall Heublein take any steps to impair United's economic and financial position. [193]

V

It is further ordered, That within twenty (20) days of the effective date of this Order, United shall be maintained and operated as a

separate corporation with separate books and accounts, separate management, separate assets and separate personnel.

VI

It is further ordered, That no substantial property or other assets of United or its subsidiaries shall be sold, leased, otherwise disposed of, encumbered, other than in the normal course of business, without the written consent of the Federal Trade Commission, and Heublein shall not commingle any assets owned or controlled by United with any assets owned or controlled by Heublein.

VII

It is further ordered, That, in complying with the requirements of Paragraph II, none of the property or business of United shall be divested to anyone who is an officer, director, or in any other way controlled or influenced by Heublein, or to anyone who owns or controls, directly or indirectly, more than 1 percent of the outstanding capital stock of Heublein or to anyone who is not approved in advance by the Federal Trade Commission.

VIII

It is further ordered, That Heublein shall, within thirty (30) days from the effective date of this Order and every sixty (60) days thereafter until Heublein has fully complied with the provisions of this Order, submit, in writing, to the Federal Trade Commission a report setting forth in detail the manner and form in which Heublein intends to comply, is complying, or has complied with this Order. All compliance reports shall include, among other things that are from time to time required, (a) the steps taken by Heublein to accomplish the required divestiture, and (b) copies of all documents, reports, memoranda, communications and correspondence concerning or relating to the divestiture. Heublein shall on the first anniversary of the effective date of this Order, and upon each anniversary date thereafter until the expiration of the prohibitions set forth in Paragraph III, submit a report, in writing, listing all of its acquisitions of or mergers with other concerns engaged in the United States wine industry, the date of each such acquisition or merger, the products involved and such additional information as may from time to time be required by the Federal Trade Commission or its staff. [194]

IX

It is further ordered, That respondent Heublein notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondent such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any change in the corporation that may affect compliance obligations arising out of this Order.

Opinion of the Commission

By Pitofsky, *Commissioner:*

The question here is whether the acquisition by Heublein, Inc. ("Heublein") of a controlling interest in United Vintners, Inc. ("United") violated Section 7 of the Clayton Act[1] and Section 5 of the Federal Trade Commission Act.[2] The amended complaint, issued in November 1972*, charged that the effect of the acquisition "may be substantially to lessen competition or to tend to create a monopoly in the production, distribution and/or sale of wine" in the United States. [2]

The amended complaint challenged the acquisition on a horizontal and several conglomerate theories, alleging that it: (i) eliminated actual existing competition between Heublein and United; (ii) eliminated the likely entry of Heublein into the wine market by the acquisition of a firm with a smaller market share than United; and (iii) would unduly entrench United's position as a market leader. The administrative law judge ("ALJ") found a violation based upon each of these three theories and ordered divestiture. We disagree, and, finding no violation of the antitrust laws, order the dismissal of the amended complaint.

As to the theories of horizontal anticompetitive effects, we find the small lessening of actual competition resulting from the merger was insufficient to establish a violation of Section 7. Similarly, with respect to the conglomerate theories, we find that the evidence in the record simply falls short of establishing a violation.

I. THE MERGING PARTIES AND THE INDUSTRY

Heublein is primarily a manufacturer, importer and marketer of alcoholic beverages. In 1968, the year prior to the acquisition,

[1] 15 U.S.C. 18.

[2] 15 U.S.C. 45.

* Amended Complaint issued November 16, 1976.

Heublein ranked as the fifth largest domestic producer of such beverages, I.D.F. 15,[3] earning a net income of $14,567,000 on net sales of $383,972,000. I.D.F. 17.[4] Distilled spirits and beer were Heublein's principal product lines; distilled spirits (mainly Smirnoff vodka) providing 52% and beer 39% of its 1968 sales. I.D.F. 16. Wine, a less significant product line, provided $14,371,000 of the 1968 sales. CX 135 B. At that time Heublein, principally an importer, sold approximately 1,685,400 gallons of wine making it the sixteenth largest seller of wines in the United States. CX 373 D, E. [3]

Prior to the acquisition, United produced and marketed numerous lines of wine—its best known brands being Italian Swiss Colony, Petri and Inglenook. In 1968 United sold approximately 38,226,000 gallons of wine, making it the second largest seller of wines in the United States. I.D.F. 498; CX 373. Its income in that year totaled $3,301,356 on net sales of $96,009,189. I.D.F. 165, 166.

Heublein acquired United at a time of rapid growth in the wine industry. Americans consumed an estimated 158.1 million gallons of wine in 1960; by 1968 that figure had risen to 205.1 million. I.D.F. 1. They spent an estimated $751 million on wine in 1960; by 1968 that figure had risen to $1,053 million. I.D.F. 2. This rapid growth continued into the following decade. American wine consumption had increased to 390.4 million gallons by 1977, and expenditures to $3 billion. I.D.F. 1, 2. Although this growth in consumption encouraged new entry in the market, I.D.F. 770, 776, the market has remained moderately concentrated. In 1968, the top four firms accounted for 47.9% of wine shipments, with the top two firms—Gallo and United—controlling 41.9%. I.D. 11.

II. THE RELEVANT MARKET

The Administrative Law Judge found, in accord with the stipulation of the parties, that the United States is the relevant geographic market for assessing the legality of the merger. He also found that one relevant product market is the "all wine" market, a market composed of the four basic types of wine: (1) sparkling, or efferves-

[3] The following abbreviations are used herein:

I.D.F. – Initial Decision Finding of Fact No.
I.D. – Initial Decision Page No.
Tr. – Transcript of Testimony Page No.
CX – Complaint Counsel's Exhibit No.
RX – Respondent's Exhibit No.
RR – Respondent's Reply to Complaint Counsel's Proposed Findings of Fact
CAB – Complaint Counsel's Appeal Brief Page No.
RRAB – Respondent's Reply Appeal Brief Page No.

[4] Heublein acquired 82% of the stock of United in September 1968 for about $33 million. I.D.F. 263. In August 1978, Heublein acquired the remainder.

cent wines; (2) still wines containing up to 14% alcohol, commonly called table wines; (3) still wines containing over 14% alcohol, commonly called dessert wines; and (4) refreshment wines, produced from inexpensive fruit concentrate rather than grapes.[5] As we acknowledged in *Coca Cola Bottling Co. of New York, Inc.*, [4]93 F.T.C. 110 (1979), the competitive offerings of the wine industry do "not consist of altogether homogeneous products." 93 F.T.C. at 204. But, as we stated there, those diverse products nevertheless may "appropriately be designated as a market" for antitrust analysis. 93 F.T.C. at 205. There is some significant competitive confrontation among even the most disparate wines, and there is also some supply-side interchangeability of productive facilities. Since no reason has been offered to abandon that conclusion here,[6] and since this record amply supports it, we hold that the all wine market is also appropriate in this case.

The ALJ also found that sparkling wines, table wines, and dessert wines each constituted a relevant submarket, but we do not find it necessary to reach these issues. Since the relevant concentration ratios and market shares for the acquiring and acquired companies do not substantially differ between the all wine market and these proposed submarkets, a determination of the validity of the submarkets would not affect the ultimate disposition of the case. *See Brown Shoe Co.* v. *United States*, 370 U.S. 294, 327 (1962).

III. HORIZONTAL ASPECTS OF THE MERGER

This case involves an acquisition by Heublein, a major marketer of alcoholic beverages with a very small presence in the wine market, of the second largest domestic wine company. In light of Heublein's extremely small percentage share of the market and the failure of complaint counsel to demonstrate that this percentage understates Heublein's true market significance, we cannot affirm the ALJ's finding of a violation in the horizontal line. United ranked second in the all wine market in 1968 with a share of 17.9%, and Heublein ranked sixteenth with a share of .79%. The 1968 market shares of

[5] The somewhat arbitrary categories of sparkling, table and dessert wines are used by state governments to tax wine distribution and by the industry itself to monitor production. I.D.F. 276, 331, 428, 430. The term refreshment wines is simply descriptive. Although refreshment wines are not made from grapes, as are other table wines, and contain less alcohol than other table wines (7–8% as compared to 10–14%), they are still included in the wine category for tax and statistical purposes. I.D.F. 438, 439.

[6] Although respondent apparently contested this market definition before the ALJ, insisting that there were separate markets for standard and premium quality wines, *see, e.g.*, I.D.F. 282; RR ¶ 90, this position has not been asserted here. RRAP 1.

United and Heublein in the table wine market were 15.6% and .23% and in the dessert wine market 21.0% and .54%.[7] CX 373 Although their 1968 market shares in the sparkling wine market were significantly higher, 10.7% and 7.2%, Heublein in late 1969 lowered the carbonation level of Lancers, the wine that accounted for [5] 99.7% of its sparkling wine sales, bringing it into the category of table wine, and leaving Heublein with a negligible share of the sparkling wine market. I.D. 112.[8]

At the time of the acquisition, the wine market was not highly concentrated nor was there any significant trend toward concentration. The four-firm ratio was 47.9%—falling near the lower end of any reasonable definition of "concentration."[9] The import of that four-firm ratio is amplified by the distribution of 41.9% of the market among the top two firms. Recent research has suggested that high two-firm shares may be more relevant than four-firm shares [6] in predicting interdependent anticompetitive behavior.[10] Disregarding, for the moment, other indicators of market behavior, we are willing to assume that the all wine market was sufficiently concentrated to warrant careful scrutiny of further increases but not so highly concentrated that an extremely stingent anti-merger policy is required. In light of the market share and concentration data presented here, Complaint Counsel cannot argue successfully that a prima facie violation has been shown. *See United States* v. *Philadelphia National Bank,* 374 U.S. 321 (1963).

Although market share percentages are "not conclusive indicators

[7] Since we do not find it necessary to reach the issues raised by the ALJ's definition of submarkets, we have relied upon submarket shares computed by complaint counsel.

[8] Complaint Counsel, in their appeal, challenge the ALJ's treatment of this change in carbonation level. The ALJ concluded that Heublein's premerger share of the sparkling wine market should be ignored because of the subsequent alteration of Lancers. But he did not then consider the Lancers sales in his evaluation of Heublein's share of the tablewine market. Doing so would have increased Heublein's share of the table wine market—apart from the wines of United—to .90% in 1970, the first full year after the change in carbonation. CX 373. United's table wines accounted for 14.8% in that year. CX 373. If the sales of Lancers in 1968, prior to the change, were added to Heublein's other table wine sales, it would yield a share of 1.2%. CX 373. While we agree with Complaint Counsel's criticism of the ALJ's calculations, that criticism does not alter our conclusion that this merger was not likely to substantially lessen competition in either the all wine market or any of the proposed submarkets.

[9] In *The Stanley Works,* 78 F.T.C. 1023, 1065 (1971), *aff'd,* 469 F.2d 498, 504-05, (2d Cir. 1972), *cert. denied,* 412 U.S. 928 (1973), the Commission found and the Court of Appeals agreed that four-firm concentration in this range described a concentrated market. *See also* Department of Justice Merger Guidelines, ¶¶5 and 6 (1968), 1 Trade Reg. Rep. ¶4510 at 6884 (1971) defining a market with four-firm concentration above 75% as "highly concentrated"); F. Scherer, *Industrial Market Structure and Economic Performance* 280 (2d ed. 1979) (suggests critical four-firm concentration level is between 45 and 59 percent); II P. Areeda & D. Turner, *Antitrust Law* ¶404 at 278 (1978) ("reason to believe that substantial effects generally disappear once four-firm concentration ratios fall below 50 to 55%"); J. Bain, *Industrial Organization* 131 (2d ed. 1968) (four firms controlling 50-65% reflects "high-moderate" concentration)

[10] *See* Kwoka, The Effect of Market Share Distribution on Industry Performance, 61 Review of Economics and Statistics 101 (1979).

Although this concern with two firm concentration has emerged only recently, the Commission has previously recognized that any skewing of the distribution of market share towards the leading firms may aggravate whatever lessening of competition that may result from a merger. *Warner-Lambert Co.,* 87 F.T.C. 812 (1976); Sullivan, *Handbook of the Law of Antitrust* 621 (1977).

of anticompetitive effects," *United States* v. *General Dynamics Corp.*, 415 U.S. 486, 498 (1974), we note that no decision has ever found a horizontal violation based upon so small a percentage increase in concentration. Violations have been found in two cases where there were percentage increases of approximately 1%: 1.3% in *United States* v. *Aluminum Co. of America*, 377 U.S. 271 (1964), and 1.0% in *Stanley Works* v. *FTC*, 469 F.2d 498 (2d Cir. 1972), *cert. denied*, 412 U.S. 928 (1973). But those cases differ significantly from that before us now.

First, in each case, the larger party to the merger controlled more of the market than did United; Alcoa accounted for 27.8%, and Amerock, the firm acquired by Stanley, 22–24%. Alcoa and Amerock were the largest firms in their respective markets, while United, by contrast, was second behind Gallo.

Second, the acquisitions reviewed in *Alcoa* and *Stanley Works* threatened more imminent anticompetitive effects. In *Alcoa* the market was already far more concentrated than the market here; the top two firms controlled 50% of the market, the top four 76%, and the top nine 95.7%. The Supreme Court also noted a trend toward vertical integration and elimination of small independent competitors resulting from recent mergers. 377 U.S. at 279 n.6. No comparable pre-acquisition trend exists in this case. Four-firm concentration in *Stanley Works* was approximately 50%, comparable to that of [7]the wine market but the Court of Appeals concluded that evidence of Stanley's strategy and pricing policies in other markets increased the likelihood of anticompetitive effects resulting from the small addition to concentration in the market at issue. Evidence before the Commission showed that Stanley had always sought to minimize price competition, acting as a "price leader" for every hardware product line in which its market strength permitted it to do so, and that pursuance of that policy was likely in the relevant market after the acquisition. *The Stanley Works*, 78 F.T.C. 1023, 1067-1074 (1971). According to the Second Circuit, the acquisition threatened to turn "a concentrated market manifesting limited signs of price competition into a rigid, lifeless market tending toward even greater concentration and economic enervation." 469 F.2d at 505. The record in this case contains no such evidence of past business activity by Heublein that adds an additional anticompetitive threat to an otherwise small increase in concentration in a moderately concentrated market.

A comparison with *United States* v. *Crowell, Collier and Macmillan, Inc.*, 361 F. Supp. 983 (S.D.N.Y. 1973) highlights the disparity between Heublein's acquisition of United and the mergers in *Alcoa*

and *Stanley.* The acquisition by Crowell Collier closely paralleled Heublein's. Crowell Collier, with .6% of the relevant market, acquired the leading firm in that market. The District Court refused to find a horizontal violation, even though the four firm concentration was 69.6%, and the market share of the acquired firm was 41.9%—statistics significantly higher than those in the Heublein acquisition.[11] The court emphasized that the particular conditions present in the market undermined even the superficial appearance of a horizontal lessening of competition. Among these conditions were a lack of a trend towards concentration, the absence of a likelihood of future defensive mergers, a lack of vertical integration among the competing firms, and the inability of any of the firms in the market to affect competition through control of price, due to the prevalent industry practice of sales through competitive bidding. [8]

It can also be questioned whether the market share statistics of 17.9% and .79% depict, as accurately as did the figures in *Alcoa* or *Stanley Works,* the possible reduction of competition resulting from this acquisition. The wine industry, as we observed in *Coca Cola Bottling Co.,* is comprised of disparate products. 93 F.T.C. at 204. And although variations in price, quality or sweetness do not justify the rejection of a relevant market comprised of all wines, those variations must be considered when evaluating the possible competitive effects of a merger between two wine producers. In both *Alcoa* and *Stanley Works* little disparity existed between the products of the merged firms[12] and hence the market share figures of 1.3% and 1% accurately measured the competitive confrontation between the firms that might be diminished by the merger. Heublein and United, however, sell markedly different products, and thus Heublein's market share of .79% may well overstate the actual competition between them.[13]

In 1968 United produced and marketed a wide range of wines, primarily under the Italian Swiss Colony, Petri and Inglenook brands. I.D.F. 160, 190. Heublein had three principal wine products:

[11] The Heublein-United percentages arguably fall outside even that "gray area at the edge of potential illegality" *The Pillsbury Co.,* 93 F.T.C. 966, 1039 (1979) under the Department of Justice guidelines for horizontal mergers. In a market with a four firm concentration under 75%, the guidelines suggest that an acquisition by a firm with 15-20% of the market is suspect when the acquired firm has at least 2-3%. Department of Justice, Merger Guidelines, ¶ 6 (1968), 1 Trade Reg. Rep. ¶ 4510 at 6884 (1971).

[12] In *Alcoa* the relevant market was defined as bare and insulated aluminum conductor, a product "designed almost exclusively for use by electric utilities in carrying electric power from generating plants to consumers." 377 U.S. at 273. The Court described no significant product variations among producers. In *Stanley Works,* the relevant market was stipulated by the parties as all residential and institutional cabinet hardware. 469 at 500. Although Judge Mansfield's dissent argued that an analysis of product variations reduced Stanley's 1% market share to an actual competitive overlap of .35%, the majority rejected the argument. 469 F.2d at 506.

[13] *See SKF Industries, Inc.,* [1976-79] Trade Reg. Rep. (CCH) (FTC Complaints and Orders) ¶21,595 (1979) [94 F.T.C. 6]; *Kaiser Aluminum & Chemical Corp.,* 93 F.T.C. 764 (1979); *United States* v. *Federal Company,* 403 F. Supp. 161 (W.D. Tenn. 1975).

vermouth, produced by Heublein in the United States, I.D.F. 11; Lancers, a carbonated rose produced by Rose Marie da Fonseca Sucrs. in Portugal, and solely distributed by Heublein in the United States; and Harveys Bristol Cream, a cream sherry produced by John Harvey & Sons, Ltd. in England, and also solely distributed by Heublein in the United States. [9]

Both Harveys Bristol Cream and Lancers stood high on the scale of prices in the wine industry. United's Inglenook line also commanded premium prices, but the vast majority of United's wines sold at the lower end of that scale.[14] Wine prices offer a rough guide to consumers' estimates of quality, and thus crudely delineate the areas of most intense competition for any wine along the broad spectrum of price and quality in the wine market. Most wine producers, as we noted in *Coca Cola Bottling Co.*, view "the bulk of their competition as coming from similar type wines within a narrow price range." 93 F.T.C. at 203–4. The record in this case, confirming that conclusion, reveals that the most intense competition for Heublein's premium priced Lancers and Harveys brands did not come from United's low price wines. To be sure, Harveys Bristol Cream and United's less expensive ports and sherries do compete: all are dessert wines, offering similar tastes and uses. *See* CX 63, 65, 97k; Tr. 2863–66, 2876. But the record reveals quite clearly that Harveys had achieved a unique position in the market. Heublein promoted it—and consumers apparently accepted it—as a prestigious wine especially suited for gifts and special occasions, *see* I.D.F. 34; Tr. 2082, 3801–02, 8737; CX 97 Z–17, 98B, 99G, J, K, and other wine producers considered that less expensive dessert wines provided no substantial competition. *See* Tr. 1868, 4245–46, 7218, 7316, 7512–16, 8744. Lancers occupied a somewhat similar position. Though it competed to some extent with all table and sparkling wines, Heublein had also marketed it, with apparent success, as a prestigious wine, *see* Tr. 8704; CX 107, 116B, C, Q, 120A, 125E, Z–25, Z–42, and Heublein, and other wine producers, believed that most lower priced wines offered little significant competition. *See* Tr. 465–6, 522–23, 2081–82, 7316–17; CX 129B, 352D.

The competitive distance between Heublein and United is less striking than that between Mogen David and Franzia described in *Coca Cola Bottling Co.*, 93 F.T.C. at 199. Nonetheless, our conclusions in that decision are still relevant here. To the extent that the wines of Heublein and United compete in separate segments of the broad

[14] Heublein's Harveys Bristol Cream sold for approximately $6.75 per fifth in 1968, CX 97M, and Lancers, $3.75. Tr. 8702–03. By comparison Italian Swiss Colony's burgundy, chablis and rose sold for approximately $.85 per fifth in 1968. RX 1255. Although Inglenook's brand Inglenook Estates sold its cabernet, pinot noir and chardonnay for approximately $3.50–$3.95, RX 1255, all of Inglenook's brands accounted for only .6% of all United's 1968 sales, and .1% of the all wine market. CX 227, 373.

all wine market, there is less "likelihood that this merger will increase opportunities for interdependent behavior on the selling side." 93 F.T.C. at 207. These observations are [10]not dispositive here, as they were in *Coca Cola Bottling Co.,* but they do indicate that Heublein's very low market share of .79% nevertheless may overstate the competitive overlap with United.[15]

Moreover, complaint counsel failed to prove that Heublein had special competitive potential such that its small market share understated its possible future competitive significance. In *Alcoa* the Supreme Court explained that Rome Cable's 1.3% market share did not fully reflect its competitive potential. Rome had competed aggressively, pioneered in research and sales, and developed special aptitudes and skills in the relevant product line. Complaint counsel did not establish that Heublein had comparable competitive significance in the wine market. It is true that Heublein was highly successful in product marketing. But it would distort *Alcoa's* definition of the special small competitor to make advertising or marketing, except in special circumstances not present here, a distinguishing characteristic. Heublein was not an innovative competitor. Its initial success came from sales of its principal product, Smirnoff vodka.[16] Most of its product diversification had resulted from acquisitions and distribution agreements, not research and development.[17] In the wine industry itself, Heublein had little significant aptitude, skill, or research potential at the time of the merger; its principal products, Lancers and Harveys, were imported from [11]foreign manufacturers.[18] Nor was Heublein an aggressive price competitor. Whatever competitive potential Heublein did possess was in no way unique; numerous other firms with a small

[15] We are careful, however, not to place too much reliance on the positioning of merged firms' products within a single market, or else the notion of a "market" could be eroded. We note the limited head-on competition between United and Heublein at the time of the merger only to assist us in assessing complaint counsel's contention that Heublein's .79% market share in reality understated the competitive significance of Heublein.

[16] In 1961, vodka sales accounted for approximately 75% of Heublein's gross sales. Tr. 3986–87. From 1963 to 1968, its sales of Smirnoff increased 43%. I.D.F. 47.

[17] Although Heublein had developed some successful premixed cocktails, based on work beginning at the turn of the century, *see* I.D.F. 51–53, its recent entry into new product lines had been accomplished by merger and agency agreements. Its list of acquisitions included: Arrow Liquers Corporation in 1965, a distributor of scotch, whiskeys, and brandies, I.D.F. 64; Vintage Wines in 1965, a distributor of foreign wines and spirits, I.D.F. 65; Theo Hamm Brewing Co. in 1965, I.D.F. 66; Don Q Imports in 1968, a rum distributor, I.D.F. 71; and Beaulieau Vinyards in 1969, I.D.F. 78.

The list of distribution agreements included: a 1966 agreement granting exclusive U.S. distribution rights for Bertani Italian Wines, I.D.F. 67; a 1966 agreement granting exclusive U.S. distribution rights for Jose Cuervo tequila, I.D.F. 69; a 1967 agreement granting exclusive U.S. distribution rights for Chateau St. George wines of France, I.D.F. 70; a 1968 agreement granting exclusive U.S. distribution rights for Black Velvet Canadian Whiskey, I.D.F. 75; and a 1968 agreement granting exclusive U.S. distribution rights for Kiku-Masamune Sake, Japan's leading sake. I.D.F. 76.

[18] *See* diseussion p. 8, *supra.*

share of the market could be considered equally important future competitive factors.[19]

Finally, we note that the evidence of market concentration trends does not significantly increase the likelihood of adverse competitive effects from this acquisition by a firm with a market share of less than 1%. A trend toward concentration did emerge after the acquisition. The market share of the top four firms increased from 47.9% in 1968 to 56.7% in 1971. I.D.F. 447. But that figure has fallen thereafter. The unavailability of some import data for the years after 1972 makes impossible any precise calculation of the decrease. I.D.F. 489. We will assume, for the sake of argument, the accuracy of the smaller estimate of that decline proposed by Complaint Counsel, placing four firm concentration at 54.2% in 1976. CAB 16. This data does not describe a particularly strong trend toward concentration, *see, e.g., United States* v. *Philadelphia National Bank,* 374 U.S. 321 (1963) (increase of market share of top seven firms from 61% to 90%), and, in light of the decline in recent years, it is insufficient to elevate to the level of a violation the increase in concentration resulting from this merger.[20] [12]

We conclude, after consideration of these conventional elements of horizontal merger theory, that the increase in concentration resulting from this merger is not likely to produce significant anticompetitive effects, and thus does not constitute a traditional horizontal violation of Section 7. It has been urged, however, that Heublein's .79% market share understated its competitive significance because Heublein's active consideration of other acquisitions at the time it acquired United makes it a unique potential deconcentrator of the market, and also because Heublein's strength as a liquor distributor, the popularity of its products, its access to financing, and its large advertising expenditures, adds more to United than Heublein's market share indicates. Consideration of "conglomerate" aspects—here, the possibility of Heublein's expansion by toe-hold acquisitions, and the possibility of some entrenchment of United's market position—can be useful in the analysis of horizontal mergers involving small market shares. *See Stanley Works* v. *FTC,* 469 F.2d 498 (2d Cir. 1972); *United States* v. *Wilson Sporting Goods Co.,* 288 F. Supp. 543 (N.D. Ill. 1968). But the possibility of entrenchment or a lessening of potential competition cannot be deemed significant—

[19] *See* discussion pp. 21–23, *infra.*

[20] *Cf.* Department of Justice Merger Guidelines, ¶ 7 (1968) 1 Trade Reg. Rep. (CCH) ¶ 4510 at 6884 (1971) (suggesting that acquisition of firm with 2% of market will be challenged if eight-firm concentration has increased by 7% in 5–10 year period); Sullivan, *supra* note 10, at 622 ("If, all things considered, the merger does not alone or with other factors pose a threat of excessive concentration, the mere fact that in the recent past concentration increased due to internal growth ought not to be enough to invalidate the merger.")

whether under consideration as an independent basis of violation, or as an aggravating factor in a horizontal violation—without some consideration of the settled qualifications on conglomerate merger enforcement developed by the Supreme Court. Those qualifications, after all, are not arbitrary but are tools to evaluate whether the likelihood of anticompetitive effect is significant. Since the ALJ found that this merger violated Section 7 under both entrenchment and actual potential competition theories, we will evaluate those claims on their own, before considering their significance when coupled with a horizontal theory.[21]

IV. THE ACTUAL POTENTIAL COMPETITION ASPECTS

A potential entrant's acquisition of a leading firm in a concentrated market may violate Section 7 if it is likely that the potential entrant, but for the acquisition, would have entered the market independently or by the acquisition of a smaller competitor in that market. Any such merger may lessen competition by eliminating the substantial increased [13]deconcentration or other procompetitive benefits likely to result from the presence of a new, or a newly reinvigorated competitor in the market.[22]

A potential *expander,* with only a minimal share of a concentrated market, may also violate Section 7 by acquiring a leading firm in that market if it is likely that the potential expander would otherwise have attempted to increase its market share by building new capacity or acquiring a smaller competitor. The merger lessens competition much as if the potential expander were a potential entrant not yet in the market.[23] The ALJ found that Heublein's

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[21] *See* discussion pp. 23 & 26, *infra.*

[22] The Supreme Court has expressly reserved approval of the actual potential competition doctrine. *See United States* v. *Marine Bancorporation,* 418 U.S. 602, 625 (1974); *United States* v. *Falstaff Brewing Corp.,* 410 U.S. 526, 537 (1973). But as we noted in *Brunswick Corp.*,[1979] 3 Trade Reg. Rep. (CCH) (FTC Complaints and Orders) ¶ 21,623, "the Commission, together with numerous federal courts, has endorsed the doctrine and we are confident that it eventually will receive the Supreme Court's approval." [1979] 3 Trade Reg. Rep. (CCH) (FTC Complaints and Orders) ¶ 21,623 at 21,782, [94 F.T.C. 1174 at 1267].

[23] As the Commission observed in *The Bendix Corp.*, 77 F.T.C. 731 (1970) *reversed and remanded on other grounds,* 450 F.2d 534 (6th Cir. 1971), in holding that Section 7 is violated by the elimination of potential entry by toehold acquisition as well as by internal expansion, the "form of entry" eliminated was not determinative; "what was determinative . . . [was] the actual elimination of the additional decision-making, the added capacity, and the other market stimuli which would have resulted had entry taken a procompetitive form." 77 F.T.C. at 817. If the potential expander would have built new capacity or acquired a smaller competitor, the acquisition of a market leader arguably adversely affects competition in much the same manner. While Bendix is often cited as a potential competition decision, it is less commonly noted that Bendix already had a small .35% share of the automotive filter market before its acquisition of Fram Corporation. 77 F.T.C. at 809.

acquisition of United lessened potential competition by eliminating the possibility of any such pro-competitive expansion.[24] [14]

Under the analysis outlined by the Supreme Court in *United States* v. *Marine Bancorporation,* 418 U.S. 602 (1974), and elaborated in subsequent decisions in the Courts of Appeals, approval of the ALJ's conclusion requires findings that (i) the all wine market was substantially concentrated, (ii) Heublein had the capacity, interest and economic incentive to expand, (iii) its expansion offered a substantial likelihood of producing deconcentration or other significant pro-competitive effects,[25] and (iv) that Heublein was one of the few most likely entrants or expanders and that its elimination as a result of the merger would be reasonably probable to substantially lessen competition. While close questions arise on several counts, we conclude that the record would adequately support the first three of these findings. But the record also plainly shows that Heublein was but one among an unusually large number of potential entrants and expanders. Under those circumstances, as we will discuss more fully below, we do not believe that the elimination of Heublein's potential for deconcentration would be likely to *substantially* lessen competition. Before reaching this issue, however, we will first review the evidence bearing upon the concentration of the market, the likelihood of Heublein's expanding by alternative means, and the probable effects of such expansion.

A. Likelihood of Entry and Prospects for Deconcentration

The preservation of potential competition is only important when the relevant market is concentrated.[26] Concentration ratios may be used to establish a prima facie case that the relevant market is sufficiently non-competitive to warrant the application of the actual potential entrant doctrine and the burden then falls upon the party defending the merger to show that those ratios "did not accurately depict the economic characteristics" of the market.[27] The all wine market's four firm ratio of 47.9% arguably falls at the edge of a reasonable definition of those markets where the loss through

[24] Complaint Counsel have not argued, and the ALJ did not find, that the possibility of Heublein's expansion exerted any disciplining effect upon the pricing decisions of competitors in the all wine market. Thus this case does not involve the perceived potential entry doctrine. *See, e.g., United States* v. *Falstaff Brewing Corp.*, 410 U.S. 526 (1973); Sullivan, *supra* note 10, at 633-638.

[25] *Brunswick Corp.*,[1979] 3 Trade Reg. Rep. (CCH) (FTC Complaints and Orders) ¶ 21,623 [94 F.T.C. 1174]. There is some authority, as well, that Heublein's expansion must be shown to have been likely to occur in the reasonably near future. *See BOC International, Ltd.* v. *F.T.C.*, 557 F.2d 24, 29 (2d Cir. 1977). *See also United States* v. *Siemens Corp.*,[1980] 5 Trade Reg. Rep. (CCH) ¶ 63,287 (2d Cir. 1980).

[26] *United States* v. *Marine Bancorporation,* 418 U.S. 602, 631 (1974). *See* Turner, Conglomerate Mergers & Section 7 of the Clayton Act, 78 Harv. L. Rev. 1313, 1382 (1965).

[27] *United States* v. *Marine Bancorporation,* 418 U.S. 602, 631 (1974).

merger of a potential entrant may [15]substantially lessen future competition.[28] In light of the high two firm ratio of 41.9%, we find that the actual potential entrant doctrine applies here. Respondent has offered no convincing evidence to the contrary.

We believe the record also supports the finding that it was reasonably probable that Heublein would have acquired a smaller competitor in the all wine market if the acquisition of United had not been possible.[29] In the years prior to the purchase of United, Heublein, primarily a marketer of vodka, had used acquisitions to enter the scotch, whiskey, brandy, beer and rum markets.[30] Strong economic incentives [16]encouraged the continuation of this pattern of growth into the wine market. That market was the only remaining major alcoholic beverage product market where Heublein did not fully participate.[31] The market's recent rapid growth, I.D.F. 1, 2, promised a profitable future, a promise made all the more tangible by the success Heublein had found possible with the two major wines it already sold.[32] Heublein's history of diversification into various alcoholic beverage markets suggests that wine was "a natural avenue of diversification"[33] for a company with Heublein's products and experience. Wine was distributed through the same channels as Heublein's other products, advertised and marketed in

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[28] In *United States* v. *Marine Bancorporation,* 418 U.S. 602 (1974), three firm concentration was 92%, considerably higher than here. The Commission and lower federal courts have found lower concentration ratios sufficient to apply the potential competition doctrine, *see, e.g., The Bendix Corp.,* 77 F.T.C. 731 (1970), *reversed and remanded on other grounds,* 450 F.2d 534 (6th Cir. 1971) (4 firm concentration at 80.8%); *United States* v. *Black & Decker Mfg. Co.,* 430 F. Supp. 729 (D. Md. 1976) (4 firm concentration at 77.5%); *United States* v. *Wilson Sporting Goods Co.,* 288 F. Supp. 543 (N.D. Ill. 1968) (4 firm concentration at 63%), and most decisions appear to have assumed that the lower boundary is near 50%. *See, e.g., United States* v. *Hughes Tool Co.,* 415 F. Supp. 637 (C.D. Cal. 1976) (4 firm concentration at 34% not sufficient); *United States* v. *Phillips Petroleum Co.,* 367 F. Supp. 1226 (C.D. Cal. 1973), *aff'd,* 418 U.S. 906 (1974) (4 firm concentration at 58% is sufficient); *United States* v. *Falstaff Brewing Corp.,* 383 F. Supp. 1020 (D.R.I. 1974) (on remand from Supreme Court, 4 firm concentration at 50% not sufficient). *See generally* Fox, Toehold Acquisitions, Potential Toehold Acquisitions, and Section 7 of the Clayton Act, 42 Antitrust L.J. 573 (1973) (60% is presumptively sufficient); V P. Areeda & D. Turner, *Antitrust Law* ¶ 1119 at 80 (1980) (55% is "ambiguous," must consider "other structural characteristics").

The market concentration here also falls just beyond the borders of the Department of Justice Merger Guidelines. *See* Department of Justice, Merger Guidelines, ¶ 18 (1968), 1 Trade Reg. Rep. ¶ 4510 at 6888 (1971).

[29] Although the ALJ also found that it was likely that Heublein would expand its share of the market through *de novo* construction if the acquisition of United were not possible, we find no evidence in the record to support this conclusion.

[30] *See* note 17, *supra.*

[31] *Cf. Brunswick Corporation,*[1979] 3 Trade Reg. Rep. (CCH) (FTC Complaints and Orders) ¶ 21,623 [94 F.T.C. 1174] (Yamaha's entry into U.S. outboard motor market found to be likely in part because it "was practically the only significant part of the world in which Yamaha was not selling substantial numbers of outboards at all").

[32] From 1963 until 1968, sales of Lancers had increased 294%, and Harveys Bristol Cream, 84%. I.D.F. 787.

[33] *FTC* v. *Procter & Gamble Co.,* 386 U.S. 568, 580 (1967). *Cf. The Bendix Corp.,* 77 F.T.C. 731, 815 (1970), *reversed and remanded on other grounds,* 450 F.2d 534 (6th Cir. 1971). ("the whole logic of Bendix's corporate development . . . and the unambiguous direction of its business growth, all pointed to expansion" into the relevant market).

the same manner, and called for management expertise not unlike Heublein's experience with similar products.[34]

There is also evidence that Heublein, recognizing these economic incentives, had a significant interest in expanding in the wine market. Heublein's acquisition of United is, of course, some evidence of Heublein's interest in the market. But that evidence is of little use in predicting whether Heublein would have purchased a smaller competitor if the United acquisition could not occur. More relevant is the evidence of Heublein's interest, throughout the years preceding the United acquisition, in wine companies having a significantly smaller market share than United. Few corporate policy documents trace this interest, but such evidence should not be necessary where, as here, there is objective evidence that a toehold acquisition or *de novo* [17]expansion would have been likely. Here, in fact, the record evidence of discussions and negotiations with possible acquisition candidates reveals significant interest in the relevant market.

During the late 1960's, the period of Heublein's diversification into numerous alcoholic beverage markets, Heublein also acquired or attempted to acquire several small wine companies. In 1965, three years before the United acquisition, Heublein expressed an interest in acquisition to both the Taylor Wine Co. and Almaden Vineyards, but neither was then available. CX 165–69, 139–42. When Almaden did become available in 1967, Heublein made an unsuccessful bid. CX 144–47. These attempts to enter the market prior to the acquisition of United provide persuasive evidence of Heublein's interest in the market.[35] Heublein had not adopted a policy of "gathering information and watchful waiting,"[36] but rather was actively seeking acquisitions. This evidence also rebuts Respondents' claim that any firm with a smaller market share than United would not have been an acceptable acquisition candidate. Such declarations of an intention to acquire only a market leader, whether drawn from corporate documents or elicited from management at trial, are not highly probative in an actual potential competition case. They offer little help in answering the central question—whether the Respondent would have entered the market by alternative means if the challenged acquisition were prohibited.[37] In this case, Heublein's

[34] *Cf. FTC* v. *Procter & Gamble Co.*, 386 U.S. 568, 580 (1967) (entry into bleach market likely because bleach "is complementary to Proctor's products, is sold to the same customers through the same channels, and is advertised and merchandized in the same manner").

[35] *See, e.g., Brunswick Corporation*,[1979] 3 Trade Reg. Rep. (CCH) (FTC Complaints and Orders) ¶ 21,623 [94 F.T.C. 1174]; *The Bendix Corp.*, 77 F.T.C. 731 (1970), *reversed and remanded on other grounds*, 450 F.2d 534 (6th Cir. 1971) (talks with acquisition candidates persuasive evidence, even though no offers made).

[36] *F.T.C.* v. *Atlantic Richfield Co.*, 549 F.2d 289, 297 (4th Cir. 1977).

[37] *See, e.g., United States* v. *Falstaff Brewing Corp.*, 410 U.S. 526, 575 (1973) (Marshall concurring); *British Oxygen Co., Ltd.*, 86 F.T.C. 1241, 1359 (1977), *reversed and remanded on other grounds*, 557 F.2d 24 (2d Cir. 1977).

unsuccessful overtures to Taylor and Almanden, and even the purchases of Vintage Wines and the Lancers trademark in 1965, show that Heublein was interested in smaller acquisition candidates. The record shows that in 1967 Taylor accounted for 2.8% and Almaden 2.0%, while Vintage would have accounted for approximately .53% of the all wine market. [18]

The record also shows that Heublein had the financial capacity to acquire a smaller wine company, that smaller companies were available, and that such an acquisition offered a feasible means of expanding Heublein's market share. Financial resources would have posed no obstacle to the acquisition of a smaller firm. Heublein ranked among the largest and most profitable companies in the nation.[38] And some of the same factors that provided an economic incentive for the United acquisition—Heublein's experience in the marketing and distribution of other alcohol products, for example—also support the conclusion that it would have been within Heublein's capacity to acquire and successfully run a small wine company.[39]

The record indicates that such smaller candidates were available at the time of the United acquisition, or shortly thereafter. Aside from Gallo and United, the largest firms in the market, the other leading firms each possessed approximately 2% of the market in 1968, clearly a sufficiently small share to qualify as a toehold acquisition.[40] Of this group, one firm, Guild Wineries and Distilleries, accounting for 2.1% of the market in 1968, was available at the time of the United acquisition. Guild approached Heublein with the suggestion of a merger a few months after Heublein learned of United's availability, but Heublein preferred to pursue the United deal. Tr. 4477, 4494, 4512–13.[41] [19]Two other firms in this group became available soon after the United acquisition. Roma, a firm with approximately 2% of the market in 1968 was acquired in 1971, and Franzia Brothers Inc. with 2.2% was acquired in 1973. Of the many smaller firms outside the top ten, several were available at the time of the United acquisition and several others soon thereafter.

[38] In 1967 Heublein stood 346th in the "Fortune 500" ranking of firms by sales and 76th by growth in earnings per share. In 1968 it ranked 5th by five year average profitability. I.D.F. 13–14. *Cf. United States* v. *Phillips Petroleum Company*, 367 F. Supp. 1226 (C.D. Cal. 1973), *aff'd*, 418 U.S. 906 (1974).

[39] *See The Bendix Corp.*, 77 F.T.C. 731, 823 (1970), *reversed and remanded on other grounds*, 450 F.2d 534 (6th Cir. 1971).

[40] *See, e.g., Missouri Portland Cement Co.* v. *Cargill, Incorporated*, 498 F.2d 851 (2d Cir.), *cert. denied*, 419 U.S. 883 (1974) (firm with 10% too large to be a toehold); *United States* v. *Black & Decker Mfg. Co.*, 430 F. Supp. 729, 767–68 (D. Md. 1976); Turner, *supra* note 26, at 1367–70.

[41] Mogen David Wine Corp., accounting for 2.5% of the market also approached Heublein with a merger proposal during this period, and Heublein again decided not to pursue the possibility. CX 197–203. But given the uniqueness of Mogen David's products, *see Coca Cola Bottling Co. of New York, Inc.*, 93 F.T.C. 110 (1979), it may have offered a less viable base for expansion in the all wine market.

San Martin Winery with approximately .21% of the market in 1967 approached Heublein with a proposal for merger in 1968, but Heublein preferred to pursue the United acquisition. CX 185-90, 373. Beaulieu Vineyard, with approximately .14% of the market in 1969, was actually acquired by Heublein a few months after United. I.D.F. 78; CX 373. During the four years following the United acquisition, a total of fifteen small firms became available and were acquired by companies other than Heublein. CX 299.

While it is true that none of these firms offered the substantial market share of United, the record offers persuasive evidence that the market share of a smaller firm could be expanded by an acquiring company and thereby contribute to deconcentration. After its acquisition of Almaden in 1967, National Distillers & Chemical Corp. was able to triple Almaden's sales by 1972; its market share doubled, increasing from 2.0% to 3.9%. CX 373. Heublein itself was able to increase Inglenook's sales over five fold during that same period. CX 227. This is persuasive evidence that the acquisition and expansion of one or more small wineries offered a viable alternative route for Heublein.[42] It also indicates that Heublein's acquisition of a smaller firm, instead of United, offered a substantial likelihood of ultimately producing some deconcentration and increased competition.[43]

B. Was There a Probability of a Substantial Lessening of Competition?

Assuming Heublein had the capacity, interest, and economic incentive to expand by acquisition of a smaller competitor, and that such acquisition would have produced pro-competitive effects in a concentrated market, it still does not follow that the acquisition of United would constitute a violation. Section 7 is concerned with the probability [20]of a substantial lessening of competition, and the elimination of a potential entrant or expander leads to a substantial anticompetitive effect only when there is a limited number of other firms reasonably likely to enter or expand in the relevant market.

The reason we are concerned about the size of the universe of entrants goes back to first principles about protection of potential competition. Essentially, we are concerned about the possibility that active competitors in a market, by agreement or tacit collusion, will raise price, diminish product quality, or otherwise fail to respond

[42] *See United States* v. *Phillips Petroleum Co.*, 367 F. Supp. 1226, 1247 (C.D. Cal. 1973), *cert. denied*, 418 U.S. 906 (1974) (relying upon similar evidence to show feasibility of toehold acquisitions).

[43] *See BOC International, Ltd.* v. *F.T.C.*, 557 F.2d 23, 27 (2d Cir. 1977); Fox, *supra* note 28, at 581 (both suggesting that this branch of the *Marine Bancorporation* test requires no elaborate factual proof).

independently to competitive pressures. If any of these things occurred, there would be an incentive for potential competitors to enter or expand in the imperfectly competitive market, and Section 7 is enforced to assure that any such potential competition is not removed by merger. But if there are many other firms roughly as capable and qualified as the party to the merger, and sharing similar incentives to expand from existing toeholds or to enter *de novo,* elimination of any single company as a potential deconcentrator normally will have no significant anticompetitive effect.[44]

Under this analysis, Heublein's elimination is insignificant in competitive terms because the record demonstrates the existence of an unusually large number of strong companies who either made toehold acquisitions or were willing and able to do so at about the time Heublein acquired United.

Two preliminary points warrant consideration here. First, in weighing the evidence on this issue, we place the burden of persuasion upon Complaint Counsel.[45] Since a merger eliminating a potential deconcentrator is anticompetitive only when the universe of other potential deconcentrators [21]is limited, proof of the point belongs upon the party challenging the merger. It would be impractical, however, to require Complaint Counsel to bear the burden of coming forward as well. Proving the negative of this proposition—proving, in other words, that no or only a few other firms were likely potential deconcentrators—would be too burdensome a requirement to be an element of the prima facie case. So we place upon the party defending the merger the initial responsibility of coming forward with evidence that a group of plausibly qualified potential deconcentrators exists. That burden is not discharged simply by naming a long list of companies who might have entered and then leaving it to the plaintiff to disprove the likelihood of entry with respect to each. Rather, the party defending the merger must be able to point to objective factors indicating that the designated firms will likely be willing and able to enter or expand if the market becomes less competitive. Once that has been done, the issue is raised and Complaint Counsel bear the burden of persuading that the universe of potential deconcentrators is limited.

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[44] *See, e.g., F.T.C.* v. *Atlantic Richfield Co.*, 549 F.2d 289, 300 (4th Cir. 1977); *Missouri Portland Cement Co.* v. *Cargill, Incorporated*, 498 F.2d 851 (2d Cir.), *cert. denied*, 419 U.S. 883 (1974); *United States* v. *Crowell Collier & Macmillan, Inc.*, 361 F. Supp. 983 (S.D.N.Y. 1973); Turner, *supra* note 26, at 1382 (if other potential entrants numerous, loss of one insignificant under an actual potential competition theory); *cf. FTC* v. *Procter & Gamble Co.*, 386 U.S. 568 (1967); *Beatrice Foods Company*, 86 F.T.C. 1, 63 (1975), *aff'd*, 540 F.2d 303 (7th Cir. 1976); *United States* v. *Hughes Tool Co.*, 415 F. Supp. 637 (C.D. Cal. 1976) (if other potential entrants numerous, loss of one insignificant under perceived potential competition theory).

[45] On this question of distribution of burdens of proof we follow the suggested approach in V P. Areeda & D. Turner, *supra* note 28, ¶ 1123a at 124–5. *See generally* James, Jr., Burdens of Proof, 47 Va. L. Rev. 51 (1961).

A second preliminary point concerns the definition of factors indicating the likelihood of entry by other outside firms. The membership of the group of other potential deconcentrators should be defined by similar criteria and kinds of evidence as are used to find that the firm at issue was likely to enter or expand. Less certainty of proof should be required with respect to these other firms, however, because the record usually will disclose far less about them than about the parties to the merger at issue.

Firms selling similar products as the firm at issue, and standing in a similar relation to the relevant market—in this case, firms already holding a toehold position in the wine market—would be the most obvious potential expanders.[46] The record here shows that nine major firms selling liquor also had a small share of the wine market at the time of the United acquisition: (1) Joseph E. Seagram & Sons, Inc. (2.5% of the all wine market); (2) National Distillers & Chemical Co. (2.3% of the all wine market); (3) Brown-Forman Distillers Corp. (2.9% of the table wine market); (4) Schieffelin & Co. (.69% of the table wine market); (5) Renfield Importers, Ltd. (.95% of the all wine market); (6) Foremost-McKesson, Inc. (percentage not available); (7) Liggett & Myers, Inc. (.24% of the table wine market); (8) Schenley Industries (2.9% of the all wine market); [22]and (9) Hiram Walker, Gooderham & Warts, Ltd. (percentage not available). All of these firms are of substantial size and likely to have had the same incentive as Heublein to expand their share of the wine market. Although some were financially smaller than Heublein, that does not necessarily make them less likely to expand; all were of substantial size and the capital markets are available to fund potentially profitable ventures.[47]

This list of potential deconcentrators is already formidable, but its criteria are nonetheless probably too narrow. We see little reason for limiting the group of potential entrants to other alcoholic beverage companies with experience in the wine market, since any acquirer could probably count on the acquired company to supply whatever "experience" would be needed. There is thus little basis for arguing that a firm competing in the liquor or beer market and interested in the wine market, but lacking experience there, is significantly less likely to acquire a wine company than a liquor or beer firm already competing in the wine market. A more reasonable definition of the universe of potential entrants in this case may therefore also include liquor or beer companies outside, but with some interest in, the wine

[46] *See generally* Sullivan, *supra* note 10 at 634; V P. Areeda & D. Turner, *supra* note 28, ¶ 1123 at 124–34; Brodley, Potential Competition Mergers, 87 Yale L.J. 1,75–77 (1977).

[47] V P. Areeda & D. Turner, *supra* note 28, ¶ 1123 at 137.

market. The record shows that at least five liquor or beer companies actually entered the wine market by toehold acquisition shortly after 1968: (1) Glenmore Distillers Company; (2) Joseph Schlitz Brewing Company; (3) Scottish & Newcastle Brewers, Ltd.; (4) Northwest Distillers; and (5) Norton Simon, Inc. Since these firms did enter shortly after 1968, it is highly likely they had the capacity, interest and economic incentive to do so at the time Heublein was removed from the list of potential entrants. The number of such firms who did not actually enter, but could have been similarly characterized as likely to enter, is probably larger.

This logic carries further. In this case there is little rational basis for limiting the list of potential deconcentrators to firms with experience in the liquor or beer markets. Seven large firms with experience in neither market actually entered the wine market by acquisition shortly after 1968: (1) Coca Cola Inc.; (2) The Nestle Company; (3) Standard Brands; (4) Pillsbury Company; (5) Pepsico, Inc.; (6) Beatrice Foods Company; and (7) United States Tobacco Co. [23]

We emphasize that this list of potential entrants is made up of companies who either actually held a toehold position in the wine market at the time of Heublein's acquisition of United or entered that market shortly after the merger. This is not just a speculative list of potential candidates with some uncertain capacity and interest—a situation in which we would be much less likely to assume companies were part of the potential competition universe.

We need not now define the minimum number of other potential entrants that makes the loss of one an insignificant lessening of competition. The number present here is overwhelming—substantially greater than any definition that has emerged in the cases or the literature.[48] There were a total of at least 21 companies with capacity, interest and economic incentive comparable to Heublein's to enter or expand in the wine business who either were already in the product market on a toehold basis at the time Heublein acquired United, or who entered shortly before or after that acquisition. Looking at this group, we are unable to conclude that Heublein's acquisition of United would have been likely to substantially lessen competition.[49] That conclusion is buttressed by the fact that the wine market was only moderately concentrated and was rapidly expand-

[48] *See, e.g., United States* v. *Hughes Tool Company,* 415 F. Supp. 637 (C.D. Cal. 1976) (6 other potential entrants made loss of one insignificant); V P. Areeda & D. Turner, *supra* note 28, ¶ 1123 at 123–4 (1980) ("a universe exceeding three similarly well-qualified potential entrants should be presumptively sufficient to obviate concern" and "a universe of six entrants removes any plausible basis").

[49] *See, e.g., F.T.C.* v. *Atlantic Richfield Co.,* 549 F. 2d 289, 300 (4th Cir. 1977); *Missouri Portland Cement Co.* v. *Cargill, Incorporated,* 498 F.2d 851 (2d Cir.), *cert. denied,* 419 U.S. 883 (1974); *United States* v. *Crowell Collier & Macmillan, Inc.,* 361 F. Supp. 983 (S.D.N.Y. 1973).

ing. We hold, therefore, that the ALJ erred in finding a violation of Section 7 on the actual potential competition theory.

In the light of the evidence described above, it is also impossible to conclude that a horizontal violation exists on the theory that Heublein was considering acquisition of smaller companies than United, and that the possibility of toehold expansion makes it a more significant competitor than its small market would otherwise suggest. Standing as one among this large group of other firms also likely to enter or expand, Heublein is simply not a unique competitor, and the loss of its potential for deconcentrating the market is not significant. [24]

V. THE ENTRENCHMENT ASPECTS

Entrenchment analysis considers the possible anticompetitive advantages that a large acquiring firm can confer on an acquired firm over competitors in the acquired firm's market. Although *FTC* v. *Procter & Gamble Co.*, 386 U.S. 568 (1967), the seminal decision, examined only the adverse competitive effects of substantial advertising and promotional advantages bestowed upon a dominant firm in a concentrated market, the logic of the Court's analysis extends further. Arguably any substantial competitive advantage resulting from the acquiring firm's size disparity or resources may cause a merger to violate Section 7—whether the acquired firm is dominant or not—if that advantage "may substantially reduce the competitive structure of the industry by raising entry barriers and by dissuading the smaller firms from aggressively competing."[50]

The ALJ was correct, therefore, in concluding that this acquisition might violate Section 7 on an entrenchment theory even though United was not the dominant firm in the market. Adverse competitive effects conceivably could result from any significant competitive advantage gained by United even if United were not the market leader. Of course, if the acquired company is small and weak in its own market, the advantages obtained by the merger may strengthen it and probably enhance competition.

The ALJ found that the acquisition entrenched United, and thus violated Section 7, because Heublein conferred on United three significant competitive advantages: (1) the ability to obtain substantial, inexpensive financing; (2) the ability to participate in a large advertising and merchandising budget, with its attendant efficiencies; and (3) the possible leverage that Heublein's popular Smirnoff

[50] *FTC* v. *Procter & Gamble Co.*, 386 U.S. 568, 578 (1967). *See* Sullivan, *supra* note 10, at 656. ("It is the effect of entrenchment, not the particular mechanism, which is central to the *Clorox* analysis.")

vodka and other liquor products might provide to increase wine distribution and sales, either through explicit or more subtle forms of tying. Barriers to entry would therefore be raised and smaller competitors disadvantaged, the ALJ ruled. Despite recent criticism of entrenchment theories based upon such competitive effects,[51] ample precedent still holds [25]that a violation of Section 7 may be predicated upon them.[52] The ALJ was also correct, therefore, in concluding that these kinds of competitive advantages deserved careful scrutiny.

But a violation is not made out simply by arguing that an acquisition might conceivably confer some competitive advantage. Adverse competitive effects cannot be assumed; the record must prove the competitive advantage to be both reasonably likely and significant and, as a result, that competition would probably be adversely affected. Indeed, because adverse competitive effects from "entrenchment" can be rather elusive, it is particularly important that a factual basis be carefully constructed.[53] Highly relevant here would be evidence demonstrating the magnitude of the acquiring company's competitive strengths, the impact of those strengths in the market of the acquired firm, and the inability of the other firms in that market to match those strengths or otherwise compete effectively.[54] Since the record in this case does not show that any advantages conferred on United as a result of the merger would be likely to have a significant competitive effect, we hold that the ALJ incorrectly concluded that the acquisition "entrenched" United and thus violated Section 7. [26]

In light of these findings, it is also impossible to conclude that a horizontal violation exists on the theory that Heublein's competitive advantages in the wine market make it a more significant competitor than its small market share would indicate.

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[51] *See, e.g., Missouri Portland Cement Co.* v. *Cargill, Incorporated,* 498 F.2d 851, 865 (2d Cir.), *cert. denied,* 419 U.S. 883 (1974) ("more metaphorical than real"); V P. Areeda & D. Turner, *supra* note 28, ¶¶ 1103, 1105, 1109, 1134.

[52] On cheaper capital cost, *see Budd Company,* 86 F.T.C. 518 (1975); *United States* v. *Ingersoll-Rand Co.,* 320 F.2d 509 (3rd Cir. 1963); *United States* v. *International Telephone and Telegraph Corp.,* 324 F. Supp. 19 (D. Conn. 1970), *appeal dismissed,* 404 U.S. 801 (1971); on advertising advantages and efficiencies, *see FTC* v. *Procter & Gamble Co.,* 386 U.S. 568 (1967); *General Foods Corporation* v. *F.T.C.,* 386 F.2d 936 (3rd Cir. 1967), *cert. denied,* 391 U.S. 919 (1968); *United States* v. *Black & Decker Mfg. Co.,* 430 F. Supp. 729 (D. Md. 1976); and on the possibility of explicit or subtle leverage, *see Procter & Gamble Co.,* 63 F.T.C. 1465 (1963), *aff'd,* 386 U.S. 568 (1967) (only the Commission decision addressed this point); *United States* v. *Wilson Sporting Goods Co.,* 288 F. Supp. 543 (N.D. Ill. 1968). *Cf. FTC* v. *Consolidated Foods,* 380 U.S. 592 (1965) (merger creating possibility of reciprocal buying may violate Section 7).

[53] *See, e.g., Missouri Portland Cement Co.* v. *Cargill, Incorporated,* 498 F.2d 851 (2d Cir.), *cert. denied,* 419 U.S. 883 (1974); *Carrier Corp.* v. *United Technologies Corp.,* 1978–2 Trade Cas. ¶62,393 (N.D.N.Y.), *aff'd,* 1978–2 Trade Cas. ¶ 62,405 (2d Cir. 1978). *See generally* Turner, *supra* note 26, at 1352-62.

[54] *See, e.g., Sterling Drug, Inc.,* 80 F.T.C. 477 (1971); *Missouri Portland Cement Co.* v. *Cargill, Incorporated,* 498 F.2d 851 (2d Cir.), *cert. denied,* 419 U.S. 883 (1974).

A. Capital Costs

The acquisition did strengthen United's financial position. Heublein provided valuable access to new capital, and helped to arrange and participated in the financing of new production facilities. *See, e.g.,* I.D.F. 62, 63; I.D. 173-4. Heublein directly extended up to $90,000,000 in long term loans. *See, e.g.,* Tr. 2515, 8121-28; CX 555, 562.

The record does not show that at the time of the merger this new access was likely to give United a significant competitive advantage over other firms in the wine market, or that it subsequently did so. Although United did borrow heavily from Heublein, the record does not show that the cost of those loans was significantly cheaper than United had paid before the acquisition.[55] Neither does the record contain evidence that United was able to obtain financing at significantly less cost than its competitors in the wine market.[56]

The evidence does suggest that any "capital cost" advantage was highly unlikely to have existed. Many of United's competitors, as we have already noted, were owned by large distillers and conglomerates, and the financial strength of many equalled or surpassed Heublein's. At the time of the acquisition, three distillers with substantially greater sales and assets than Heublein competed in the wine [27]market: Joseph E. Seagrams & Sons, Inc., National Distillers & Chemical Corp., and Scheneley Industries.[57] And many of the firms that subsequently acquired small wine companies—Coca Cola Bottling Co., Standards Brands, Inc., Norton Simon, Inc., and Beatrice Foods Co., for example—were vast diversified enterprises whose resources dwarfed Heublein's.[58] All of these firms could have matched or surpassed any competitive advantage that Heublein's financial resources offered United. In light of their presence in the

[55] The loans from Heublein actually bore 1/2% higher interest than one of United's two major long term interest bearing loans before the acquisition. The interest rates of the loans from Heublein were set at 1% over the prime rate, CX 562; Tr. 9473; the rate of one of the preacquisition long term loans was 1/2% over the prime rate. CX-555.

[56] The record does contain evidence that in 1975 and 1976 Heublein unsuccessfully attempted to replace its own loans to United of approximately $90,000,000 with bank loans; the effort failed because no bank was willing to extend the loans without charging higher rates. *See* Tr. 8121-25, 9473-6. But this evidence alone does not answer the central question—whether Heublein's financing gave United a significant competitive advantage. The evidence may not even reflect any advantage at all, but rather only a change in conditions in the capital markets.

[57] In 1968 Joseph E. Seagrams & Sons, Inc. had sales of $1,049,593,000 and assets of $733,760,000, National Distillers & Chemical Corp., $957,645,000 and $794,965,000, and Schenley Industries, Inc. $550,348,000 and $519,929,000. RX 475, 509, 537. Heublein had sales of $383,972,000 and assets of $141,171,000. CX 49.

[58] Coca Cola, for example, had sales of $3,559,878,000 and assets of $2,223,924,000 in 1977, the year it acquired Sterling Vineyards and the Taylor Wine Co. CX 299; RX 1232. Standard Brands had sales of $1,294,989,198 and assets of $718,517,599 in 1972, the year it acquired Jullius Wile Sons & Co. CX 299; RX 518. Norton Simon had sales of $1,739,763,000 and assets of $1,418,947,000 in 1977, the year it acquired San Martin Vineyards. CX 299; RX 481. Beatrice Foods, which acquired Brookside Enterprises in 1973, had sales of $5,288,578,000 and assets of $2,128,875,000 by 1977. CX 299, RX 1232.

market, it is impossible to conclude that Heublein's ability to finance United could have substantially lessened competition.[59]

B. Advertising Efficiencies

There was no substantial evidence in the record justifying the conclusion that Heublein was likely to or did bring to United a significant competitive advantage in advertising, or that the merger was likely to or did increase barriers to entry attributable to advertising or product differentiation. While it is true that Heublein spent heavily for advertising, its expenditures, even without taking inflation into account, were far less than found in either *FTC* v. *Procter & Gamble Co.,* 386 U.S. 568 (1967) or *General Foods Corporation* v. *F.T.C.,* [28]386 F.2d 936 (3rd Cir. 1967), *cert. denied,* 391 U.S. 919 (1968), the decisions pioneering the concept that significant advertising advantages could violate Section 7.[60] More importantly, those decisions did not define large advertising expenditures alone as the threat to competition. The mergers were prohibited because the acquiring companies had access to significant advertising efficiencies—whether from access to cumulative quantity discounts or simply scale efficiency savings—unavailable to the other competitors in the acquired firm's market. Although the record in this case suggests Heublein did benefit from some such efficiencies,[61] there is no evidence whatsoever on how much was saved, nor any evidence indicating that those efficiencies were not available to the other firms in the wine market. Considering the number of other large competitors who were either in the market at the time of the United acquisition, or who entered shortly thereafter, it is highly unlikely that Heublein enjoyed any comparative advantage.

Even if Heublein had enjoyed such an advantage, the record does not show that it would have been of decisive importance or even competitively significant. Advertising was critical to a firm's success

[59] *Compare Sterling Drug Co.,* 80 F.T.C. 477 (1971); *Missouri Portland Cement Co.* v. *Cargill, Incorporated,* 498 F.2d 851 (2d Cir.), *cert. denied,* 419 U.S. 883 (1974); *United States* v. *Black & Decker Mfg. Co.,* 430 F. Supp. 729 (D. Md. 1976) *with FTC* v. *Procter & Gamble,* 386 U.S. 568 (1967).

[60] Procter & Gamble was the "nation's largest advertiser" in 1957, the year it acquired Clorox, *FTC* v. *Procter & Gamble Co.,* 386 U.S. 568, 573 (1967), and General Foods was the third largest in 1961, three years after it acquired S.O.S., *General Foods Corporation* v. *F.T.C.,* 386 F.2d 936, 938 (3rd Cir. 1967), *cert. denied,* 391 U.S. 919 (1968). Procter & Gamble's expenditures for advertising and other promotions totalled $127,000,000 in 1957, 386 U.S. at 573; General Foods totalled $69,000,000 in 1957, the year of the acquisition. 386 F.2d at 938. In 1970, two years after the United acquisition, one advertising publication described Heublein as the 44th largest advertiser in the nation, and fixed its expenditures at $40,500,000. CX 339, 331, 332. Respondent has maintained that its expenditures were even lower. CX 332.

[61] The record contains evidence, for example, that some discounts were available in purchases of local television and radio time, billboard space, and newspaper and magazine space, *see, e.g.,* Tr. 3716, 7987, 8776, 9754–55, and that significant savings could be earned by sharing advertising time or space among several products. *See, e.g.,* CX 501, 87Z–7.

in *Procter & Gamble* and *General Foods* because the product markets were composed of low priced, high turn-over items lacking significant distinguishing characteristics. The wine market differs [29] markedly in this respect from the liquid bleach or steel wool markets; it is composed, as we have already noted, of competing products varying significantly in price, quality and use. Where such product differences exist, an advantage in advertising costs is less likely to be of competitive importance.[62] It is also more likely to be competitively useful, encouraging product variations by informing consumers of a wide range of different products.

An examination of the advertising to sales ratios in the wine market bears out this observation. Especially high advertising expenditures were not necessary for Gallo and United to maintain their leading market shares in 1968 nor for National Distillers to increase Almaden's market share in the years that followed. In 1967 Gallo's advertising to sales ratio was 5.4%, and United's 6.0%. Between 1971 and 1974, the period of Almaden's market expansion, its advertising to sales ratio never exceeded 1.9%.[63] These ratios are significantly lower than those in cases where advertising has been found a critical element of market success, and thus a possible basis for entrenchment under Section 7.[64] Any advantage in advertising costs that Heublein might have brought to the wine market was thus of doubtful competitive significance.

C. Possible Tying or Leverage

Since Heublein's liquor products could be sold through the same distribution channels as United's wines, this acquisition creates the possibility that Heublein could use the popularity of Smirnoff vodka as leverage to coerce its distributors or retailers into carrying United's wines. Whether Heublein issued express threats or exerted more subtle coercion—or even if distributors and retailers voluntarily purchased United's wines to curry Heublein's favor—competition might be lessened by the restricted access to distribution channels imposed upon United's competitors. Section 7 clearly may be violated by a merger creating the possibility that the acquiring firm's reciprocal buying power will give a competitive advantage to

[62] *See, e.g., United States* v. *Black & Decker Mfg. Co.*, 430 F. Supp. 729 (D. Md. 1976); *United States* v. *Crowell Collier & Macmillan, Inc.*, 361 F. Supp. 983 (S.D.N.Y. 1973); *United States* v. *Wilson Sporting Goods Co.*, 288 F. Supp. 543 (N.D. Ill. 1968).

[63] *See* RR ¶¶ 291, 292, 331; RAB p. 67 fn.99.

[64] *See, e.g., General Foods Corp.*, 69 F.T.C. 380, 434 (1966), *aff'd*, 386 F.2d 936 (3rd Cir. 1967), *cert. denied*, 391 U.S. 919 (1968) (over 15%).

the acquired [30]firm, whether that advantage may result from explicit or subtle coercion or from voluntary actions.[65] While the issue is less clear, we will assume that Section 7 can also be violated by a merger creating the possibility of a competitive advantage arising from the leverage of a successful product of the acquiring firm.[66] This is especially true when, as here, the acquiring company has a truly desirable product—Smirnoff vodka—in a clearly related line and the acquired company's products already hold a leading market position.

Several considerations suggest, however, that the mere possibility that leverage could occur should not be sufficient to establish a violation. First, it will almost always be the case that leverage is "possible" when firms selling related products merge. At the same time, substantial efficiencies and savings can result from the integration of distribution systems following such mergers—either actual selling or distribution efficiencies or a reduction in transaction costs resulting from customers ability to do business with a single seller. A rule that outlaws mergers upon a showing of the mere possibility of leverage therefore would have significant social and economic costs.[67] Hence "leverage" should be a ground for barring an otherwise unobjectionable merger only when the evidence of probable adverse competitive effects is fairly clear. Second, since any full line forcing or tying produced by the leverage could most likely be later challenged under Section 3 of the Clayton Act or Section 1 of the Sherman Act, the anticompetitive effects that could only be eliminated by prohibiting [31]the merger will often be both insignificant and remote. They would be limited to coercion too subtle to be proven in a subsequent enforcement action, and voluntary purchases by distributors and retailers. In light of possible redeeming economic benefits of mergers integrating distribution systems, and the likelihood that in most cases few significant anticompetitive effects will result from any leverage made possible by them, we conclude that the existence of possible leverage should

[65] *See, e.g., FTC* v. *Consolidated Foods*, 380 U.S. 592 (1965); *United States* v. *Ingersoll-Rand Co.*, 320 F.2d 509 (3rd Cir. 1963); *Allis Chalmers Mfg. Co.* v. *White Consolidated Indus. Inc.*, 414 F.2d 506 (3rd Cir. 1969), *cert. denied*, 396 U.S. 1009 (1970).

[66] *See* note 52, *supra*. *See also Coca Cola Bottling Co. of New York, Inc.*, 93 F.T.C. 110 (1979); *United States* v. *International Telephone & Telegraph Corp.*, 324 F. Supp. 19 (D. Conn. 1970), *appeal dismissed*, 404 U.S. 801 (1971); Department of Justice Merger Guidelines, ¶ 20 (1968), 1 Trade Reg. Rep. ¶ 4510 at 6889 (1971).

[67] Of course, evidence of efficiencies is not admissible in individual cases in defense of an otherwise illegal merger. *See FTC* v. *Procter & Gamble*, 386 U.S. 568, 580 (1976) ("Possible economies cannot be used as a defense to illegality"). Our point rather is that in looking prospectively at what kind of across-the-board rules should be developed to treat questions of entrenchment by leverage in conglomerate cases, possible loss of efficiencies, along with many other factors, should be taken into account. *Cf. The Pillsbury Co.*, 93 F.T.C. 966 (1979).

be a ground for barring a merger only when the evidence shows that it will probably produce significant adverse competitive effects.[68]

The record in this case will not support such a finding. Smirnoff vodka might have been a powerful leverage tool, but the record contains no convincing evidence showing either that Heublein would probably have exercised that leverage, or that distributors and retailers would have purchased United's wines to win Heublein's favor and thus insure their supply of Smirnoff. There is no evidence that Heublein had ever attempted to use the leverage of any of its products prior to the acquisition of United. Neither is there any evidence that the potential for exercising leverage motivated Heublein's decision to acquire United, that Heublein ever attempted to use its leverage to increase United's sales, or even that Heublein considered it.[69] [32]

A comparison with the record supporting the Supreme Court's determination in *FTC* v. *Consolidated Foods,* 380 U.S. 592 (1965) that the use of reciprocal buying power posed a threat to competition highlights the lack of evidence in the record now before us. In that case, the Court had before it evidence that Consolidated Foods planned a program to apply its purchasing power and implemented that program with systematic coercive efforts, that some customers gave in to the coercive efforts, and that the acquired company succeeded in increasing its market share. While all of these elements need not be proven to establish a violation, the record in this case does not convincingly establish any of them. Indeed, as noted previously, United's market share was down considerably in the years following the merger.

Consideration of the marketing practices of other firms in the wine market supports the conclusion that significant anticompetitive effects were unlikely. The record contains no convincing evidence that other distillers owning wine companies had ever used the

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[68] *See* V P. Areeda & D. Turner, *supra* note 28, ¶ 1134 at 202–13 (1980); *cf. FTC* v. *Consolidated Foods,* 380 U.S. 592, 603 (1965) (Steward, J., concurring) ("Clearly the opportunity for reciprocity is not alone enough to invalidate a merger under Section 7."); *United States* v. *International Telephone & Telegraph Corp.,* 324 F. Supp. 19 (D. Conn. 1970), *appeal dismissed,* 404 U.S. 801 (1971) (must show reciprocity "is likely to occur"). *But cf. Allis Chalmers Mfg. Co.* v. *White Consolidated Indus. Inc.,* 414 F.2d 506 (3rd Cir. 1969), *cert. denied,* 396 U.S. 1009 (1970); *United States* v. *Ingersoll-Rand Co.,* 320 F.2d 509 (3rd Cir. 1969) (both preliminary injunction cases suggesting necessity only of showing reciprocity is possible).

[69] *Cf. United States* v. *International Telephone & Telegraph Corp.,* 324 F. Supp. 19 (D. Conn. 1970), *appeal dismissed,* 404 U.S. 801 (1971) (similar lack of evidenced convinced court that use of reciprocal buying power not likely).

The only evidence in the record suggesting any proclivity for using one product to increase the sales of another is found in two marketing strategy documents describing a 1971 plan to ease the introduction of a new line of United wines, the Vinya line, by requiring retailers to *substitute* some Vinya for their usual purchases of Lancers. *See* CX 115, 352. This is not the kind of leverage that displaces competitors.

leverage of their successful liquor products to increase their wine sales.[70] Neither is there any convincing evidence of substantial voluntary behavior by distributors and retailers to win the goodwill of their major suppliers to the disadvantage of smaller wine producers. If evidence of industrywide practice is to support an inference that the leverage of a particular acquiring firm is likely to be used, that evidence—in the absence of any showing that that company has used its leverage in the past or intends to use it in the future—must be more systematic than the anecdotal testimony in this record. *See, e.g.,* Tr 391, 641–53, 1044, 1057, 4960–68.

Finally, the likelihood of the strategy's appeal is diminished by the lack of evidence indicating that distributors or retailers would have been vulnerable to pressure from Heublein. There is no substantial evidence that they depended upon their major suppliers for substantial credit, leases of facilities, or sales assistance.[71] There are, indeed, [33]many indications that distributors and retailers would have been strong enough to resist any pressure directed at them if it had been attempted and that Heublein's competitors were strong enough to prevent leverage from deadening competition on increasing market concentration.

In sum, then, this record will not support the conclusion that the possibility of leveraged sales created by this acquisition was likely to have produced significant anticompetitive effects.

Final Order

This matter has been heard by the Commission upon the appeals of complaint counsel and respondent from the initial decision and upon briefs and oral argument in support of and in opposition to the appeals. For the reasons stated in the accompanying Opinion, the Commission has determined to sustain respondent's appeal. Complaint counsel's appeal is denied. The motions to supplement the record filed by respondent and complaint counsel are denied. Accordingly,

It is ordered, That the complaint is dismissed.

[70] *Cf. United States* v. *International Telephone & Telegraph Corp.,* 324 F. Supp. 19 (D. Conn. 1970), *appeal dismissed,* 404 U.S. 801 (1971) (suggesting similar evidence would be relevant to show likelihood of reciprocity power being exercised).

[71] *See United States* v. *Wilson Sporting Goods Co.,* 288 F. Supp. 543 (N.D. Ill. 1968) (dealers' dependency for credit and assistance made them vulnerable).

IN THE MATTER OF

ATLANTIC RICHFIELD COMPANY

MODIFYING ORDER IN REGARD TO ALLEGED VIOLATION OF SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT AND SEC. 7 OF THE CLAYTON ACT

Docket 9089. Order, Oct. 29, 1979—Modifying Order, Oct. 7, 1980

This order reopens the proceeding and modifies definition (h)(1) and (2) of the divestiture order issued on October 29, 1979, 44 FR 67643, 94 F.T.C. 1054, so that, upon prior Commission approval, Noranda Mines Ltd., INCO Ltd., the Anglo American Group, or any of their respective subsidiaries (previously designated as "ineligible"), may be considered as "eligible" to purchase properties to be divested or to engage in certain joint ventures with Atlantic Richfield.

ORDER REOPENING PROCEEDING AND MODIFYING CONSENT ORDER

By letter dated January 14, 1980, Noranda Mines Ltd. ("Noranda") requested that the Commission reopen this proceeding to reconsider the designation of Noranda as absolutely ineligible to purchase the properties subject to divestiture under the consent order issued in this proceeding on October 29, 1979.[1] One of the principal objectives of the consent order was to promote deconcentration of the copper industry through divestiture of the subject properties to firms that presently are not major producers. Atlantic Richfield may divest the properties to, or engage in certain joint ventures with, any person who is "eligible" under the terms of the order.[2] Because eligibility based solely on market share criteria could not meet the Commission's competition objectives in this instance, three major companies—Noranda, INCO Ltd. and the Anglo American Group—were designated by name as ineligible. Those companies' actual or potential competitive positions were believed to be inadequately reflected by reference solely to market share criteria.

Upon consideration of Noranda's request, the Commission determined that it would be in the public interest to reopen the

[1] The Commission has treated Noranda's correspondence as a request that the Commission reopen this proceeding on its own initiative, as authorized by Sections 3.71 and 3.72 of the Commission's Rules of Practice. Rules 3.71 and 3.72(b)(1), 45 F.R. 21622 (Apr. 2, 1980).

[2] To determine eligibility, the October 29 consent order defines "Eligible Person" and "Ineligible Person." It designates as absolutely ineligible any person having more than ten percent (10%) of the United States copper market for any of the three calendar years preceding an attempt to purchase the subject properties or to engage in certain joint ventures with Atlantic Richfield. Any person having between five percent (5%) and ten percent (10%) of the United States copper market for any of the three calendar years is eligible to purchase the subject properties or to engage in certain joint ventures with Atlantic Richfield only upon prior approval of the Commission. Three companies, Noranda, INCO Ltd. and the Anglo American Group, are declared absolutely ineligible. Definitions (h) and (i) of the order.

proceeding for the purpose of modifying the consent order. The Commission was of the opinion that the public interest in improving competition in the copper industry may adequately be served by designating Noranda, INCO Ltd. and the Anglo American Group as eligible upon prior approval of the Commission.[3] On June 19, 1980, the Commission issued an order to show cause why the consent order should not be modified. The show cause order invited interested persons to comment on the proposed change.

Having carefully considered the comments received,[4] the Commission continues to believe that the competitive positions of Noranda, INCO Ltd. and the Anglo American Group are not adequately reflected by reference solely to market share criteria. The Commission has concluded that the public interest would adequately be served by giving each of the three firms an opportunity to present its views in the context of a specific request for prior Commission approval of a proposed divestiture transaction or a proposed joint venture subject to Paragraphs IX and X of the consent order.

Now, therefore, it is hereby ordered, pursuant to Section 5(b) of the Federal Trade Commission Act, 15 U.S.C. 45(b), and Rule 3.72(b) of the Commission's Rules of Practice, 16 C.F.R. 3.72(b) (1979), that the October 29, 1979 consent order be modified in part as follows (new language is italicized, deleted language is hyphened out):

For purposes of this Order, the following definitions shall apply:

* * * * * * *

(h) (1) Subject to the provisions of subparagraph (2) of this definition "h", "Eligible Person" means all Persons ~~other than Noranda Mines Ltd., INCO Ltd., the Anglo American Group, and any of their respective subsidiaries, and any other Person~~ having *not* more than ten percent (10%) of the Copper Market for any of the three calendar years immediately preceding (i) an attempt by such Person to acquire a property or interest to be divested under the provisions of Paragraphs I through V of this Order, or (ii) an attempt by such Person to enter into a Joint Venture with Respondent which may be subject to the provisions of Paragraphs IX and X of this Order. ~~The "Anglo American Group" means the Anglo American Corporation of South Africa Limited, Charter Consolidated Ltd., De Beers Consolidated Mines Ltd., Hudson Bay Mining and Smelting Co., Limited, Minerals and Resources Corporation Ltd., Anglo American Corporation of Canada Limited, and Inspiration Consolidated Copper Company and their respective subsidiaries.~~

(2) *Noranda Mines Ltd., INCO Ltd., the Anglo American Group, and any of their respective subsidiaries, and any* Person otherwise eligible under subparagraph (1) of

[3] Although Noranda is the only one of the three companies that has requested a reopening of this proceeding, its position is not substantially different from that of INCO Ltd. or the Anglo American Group. Therefore, the Commission has concluded that it would be appropriate to modify the order with respect to all three firms.

[4] Comments were received from Noranda and from respondent Atlantic Richfield. Noranda proposed an alternative modification. Atlantic Richfield stated that it does not object to the Commission's proposed modification.

this definition "h" having between five percent (5%) and ten percent (10%) of the Copper Market for any of the three calendar years immediately preceding any of the events described in sections (i) and (ii) of subparagraphs (1) of this definition "h", shall be considered to be an "Eligible Person" only upon prior approval of the Commission. *The "Anglo American Group" means the Anglo American Corporation of South Africa Limited, Charter Consolidated Ltd., De Beers Consolidated Mines Ltd., Hudson Bay Mining and Smelting Co., Limited, Minerals and Resources Corporation Ltd., Anglo American Corporation of Canada Limited, and Inspiration Consolidated Copper Company and their respective subsidiaries.*

IN THE MATTER OF

ZAYRE CORPORATION

MODIFYING ORDER IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C–2908. Decision, Oct. 27, 1977—Modifying Order, Oct. 8, 1980

This order reopens the proceeding and modifies the order issued against the firm on October 27, 1977, 42 FR 60138, 90 F.T.C. 329, in connection with the availability and pricing of advertised specials. In conformity with the modification allowed on April 9, 1980 to the order issued against Pay'N Pak Stores, Inc., Docket C-2780, the order requires only a limited disclosure of availability where closeout merchandise is involved (merchandise whose entire inventory is being disposed of at a reduced price and which is not planned to be restocked).

ORDER REOPENING THE PROCEEDING AND MODIFYING DECISION AND ORDER

On October 27, 1977, the Commission issued a Decision and Order against Zayre Corp. in connection with the availability and pricing of advertised specials. The Order includes a provision to prevent Zayre from representing in its advertisements that merchandise is available at its stores at any price unless each advertised item is readily available for sale at or below the advertised price and that each advertised item is properly marked. There are certain exceptions to the availability and pricing requirements of the Order.

On July 18, 1980, Zayre Corp. petitioned the Commission pursuant to Section 5(b) of the Federal Trade Commission Act, as amended on May 28, 1980, and Section 2.51 of the Commission's Organization, Procedures and Rules of Practice, 16 C.F.R. 2.51, to reopen the proceeding for the limited purpose of modifying the consent order in conformity with the modification allowed on April 9, 1980, to the Order issued against *Pay'N Pak Stores, Inc.,* Docket C–2780, dealing with "closeout" merchandise. On August 15, 1980, Zayre filed supplemental papers with respect to its petition.

"Closeout" merchandise was defined in the modified Pay'N Pak order as merchandise whose entire inventory is being disposed of at a reduced price and which is not planned to be restocked. Zayre's proposal embodies the same definition. It would, as the Pay'N Pak order, require only a limited disclosure of availability where closeout merchandise is involved.

After due consideration, the Commission believes that the public interest will be served by modifying the Zayre Corp. Decision and

Order to allow a general availability limitation on "closeout" merchandise.

It is ordered, That the proceeding is reopened.

It is further ordered, That the Zayre Corp. Decision and Order issued on October 27, 1977, is modified as follows:

The following paragraph is to be inserted after the first subparagraph in Section 2(b) of the Order which concludes with the words "rain check.":

For closeout items, in instances where an advertisement is for more than one store, the quantity limitation will be deemed to be complied with by disclosures that the items are closeout items and that the 'quantities are limited to stock on hand'. Closeout designation is only appropriate for items where Zayre both is disposing of the entire inventory of an item at a reduced price and is not planning on restocking the item.

IN THE MATTER OF

KELLOGG COMPANY, ET AL.

Docket 8883. Interlocutory Order, Oct. 9, 1980

ORDER DENYING IN PART MOTION TO DISMISS AND DIRECTING THE FILING OF A REPORT AND OF SUBSEQUENT BRIEFS

In its Order of July 31, 1980, the Commission deferred ruling on one portion of the motion of General Foods Corporation ("General Foods") dated April 3, 1980, for dismissal of the complaint in this matter.[1] In this portion of its motion General Foods contends that the Commission has deprived it of due process of law "by impermissibly intermingling its prosecutorial, administrative and judicial functions to the point where the prosecution formulated the course which the Commission then followed." Motion at 2. In the alternative, General Foods seeks a full evidentiary hearing into the matters raised in its motion.

General Foods contends that dismissal of the complaint is required because of the "improper and prejudicial" participation of former chief administrative law judge Daniel Hanscom and of officials of the Bureau of Competition "in determining Judge Hinkes' status." Memorandum of General Foods Corporation (1) In Support of its Motion to Dismiss the Complaint, and (2) In Response to the Federal Trade Commission Order of March 4, 1980 ("Memorandum") at 38. In our order of July 31, we noted that this contention had not previously been raised, and before addressing it we determined to augment the record by obtaining affidavits from those who appeared best able to provide evidence relevant to the negotiation process with Judge Hinkes and the role of Bureau of Competition officials in that process. In compliance with our order, Messrs. Daniel C. Schwartz, Peter Brickfield, Barry R. Rubin, John F. Dugan and Barry Kefauver have filed affidavits.[2] Having reviewed these affidavits, Mr. Kefauver's affidavit of December 13, 1979, Judge Hanscom's affidavit of December 5, 1979, and certain additional material, discussed in Part II of this order, we have determined (1) to deny the reserved portion of General Foods' motion of April 3, 1979, insofar as it relates to the activities of Judge Hanscom; (2) to defer disposition of that portion of the motion insofar as it relates to the activities of officials of the Bureau of Competition; (3) to direct the Bureau of Competition to file the report specified in Part II of this order; and (4) to direct the parties to file their views on the need for additional factfinding.

[1] The motion was in other respects denied in our order of July 31.

[2] By memorandum of August 21, 1980, Mr. Rubin corrected typographical errors in his affidavit.

I.

General Foods asserts that Judge Hanscom, in his former capacity as Assistant Director for Evaluation in the Bureau of Competition, had signed and approved the memorandum to the Commission recommending issuance of the complaint in this proceeding. Memorandum at 35. While the memorandum recommending the complaint is not part of the record in this adjudication, General Foods' assertion is evidently correct.[3] Having acted in this prosecutorial capacity, Judge Hanscom was disqualified from participating in adjudicative decision-making in the proceeding. 5 U.S.C. 554(d).[4] The question, therefore, is whether Judge Hanscom's participation in the process leading up to the contract with Judge Hinkes violated this separation of functions requirement, or whether it was a permissible involvement in an administrative decision divorced from the merits of the proceeding.

We held, in our order of July 31, that Judge Hanscom could properly appoint a successor to Judge Hinkes, though he is disqualified from the adjudication. Order at 13. As noted in our order, the Commission some years ago held that the Chairman, who was not participating in the adjudication in question, might nevertheless properly exercise his discretion as administrative head of the agency in the decision whether to seek to retain an ALJ in the very proceeding as a retired annuitant. *Hearst Corp.*, 81 F.T.C. 1028, 1029 (1972).

This distinction between adjudicative and administrative decision-making will inevitably be clearer in some instances than in others. Whenever a decisionmaker acts in his or her administrative capacity, and that decision directly relates to the adjudication, as would always be true of a decision on retention of an ALJ, the action will perhaps inescapably be susceptible to the accusation of improper motive. But suspicion alone is not enough. Officials who routinely make administrative decisions of a particular kind will not be held to have exceeded the proper scope of their authority without clear evidence of impropriety.

The evidence here falls short. There is not the slightest suggestion in the record that Judge Hanscom recommended the contract out of any belief that retention of Judge Hinkes in the *Kellogg* case would result in rulings favorable either to complaint counsel or to respondents.

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[3] In a colloquy at a hearing in November, 1977, complaint counsel identified Judge Hanscom as one of the signatories of the memorandum. Tr. 26281.

[4] "An employee or agent engaged in the performance of investigative or prosecuting functions for an agency in a case may not, in that or a factually related case, participate or advise in the decision * * *."

Instead, the record reflects that Judge Hanscom's only concern was that if Judge Hinkes left the case, a retrial might be required, at enormous expenditure, which could do little more than replicate the record that had already been before Judge Hinkes. Such a concern is not, as General Foods claims, a "direct, partisan interest in preserving the consequences of [Judge Hanscom's] earlier involvement," because it is not in any way addressed to the merits of the adjudication. Rather, it is a purely administrative concern that public resources not be wasted on duplicative proceedings. It follows from these facts that as a matter of law, Judge Hanscom's action involving the contract with Judge Hinkes did not amount to participation in the decisionmaking process of the adjudication, within the meaning of the applicable restriction in 5 U.S.C. 554(d).[5]

Even if it be assumed that Judge Hanscom's participation in the negotiations and his recommendations to the Chairman violated the separation of functions requirement in the Administrative Procedure Act, we hold that the remedy of dismissal sought by General Foods is altogether inappropriate and unnecessary. If the contract with Judge Hinkes was fundamentally flawed because of Judge Hanscom's involvement in the process leading up to it, as General Foods alleges, then the remedy would be removal of Judge Hinkes, which indeed is what General Foods urged when it first contended that the contract was improper. Motion of General Foods Corporation to Disqualify the Administrative Law Judge, dated October 13, 1978. The Chairman's decision of December 8, 1978, not to submit the contract to the Civil Service Commission for approval, together with the Commission's order of the same date holding that, in the circumstances, Judge Hinkes had become unavailable within the meaning of 5 U.S.C. 554(d) as of the date of his retirement, had precisely the effect of removing Judge Hinkes from the proceeding. Thus we conclude that, even if we were to accept (which we do not) that Judge Hanscom erred in recommending the contract, General Foods has not been prejudiced, for any arguable harm has been ameliorated by the removal of Judge Hinkes.

II.

With respect to the contentions of General Foods about the role of officials of the Bureau of Competition in the process leading to the offer of the contract to Judge Hinkes, we have concluded that more evidence is needed before we can rule.

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[5] Insofar as General Foods intends to suggest that Judge Hanscom's actions were unlawful under any of the theories outlined on pages 43 to 46 of its Memorandum, we find that suggestion to be wholly without merit.

As we indicated in our order of July 31, the purpose of the ancillary inquiry now is to establish facts sufficient to permit our disposition of allegations that officials of the Bureau of Competition violated the Commission's *ex parte* rule, Rules of Practice Section 4.7, or otherwise improperly breached the separation of functions requirement of the Administrative Procedure Act, 5 U.S.C. 554(d). The affidavits submitted in response to that order, together with materials previously entered in the record, provide an account of the Bureau's involvement from August 14, 1978, in the negotiation process that culminated in the contract with Judge Hinkes. With one exception,[6] the Commission concludes that no further factual development is necessary at this time with respect to the actions of the various participants in the process from August 14, 1978, on.

However, the affidavits do not establish how officials of the Bureau first learned that Judge Hinkes was contemplating retirement. Mr. Schwartz states that he "first learned of Judge Hinkes' contemplated retirement from members of the staff of the Bureau of Competition on or about the date of the meeting which was held on August 14, 1978, * * *." Schwartz Aff. ¶ 1; see also *id.* ¶ 4. He does not state who the "members of the staff" were.

There is a second ground for our continuing the inquiry. It arises from material brought to the Commission's attention by the General Counsel. In the course of preparing the Commission's defense to an action brought by Kellogg Co. on July 24, 1980, under the Freedom of Information Act for, *inter alia,* documents referring or relating to the employment of law judges who have stated an intention to leave their regular law judge position, and for documents referring or relating to any policy or practice of the Commission regarding actions to be taken by Commission employees upon an ALJ's leaving or stating an intention to leave, the staff of the General Counsel's office undertook a thorough canvass to be certain that all responsive documents had been located. In the course of that search, the General Counsel obtained, from the files of complaint counsel, documents which appeared relevant to this ancillary inquiry. The General Counsel brought these documents to our attention, and we now direct that they be placed on the record.

The first document is a memorandum to the file from Anthony Low Joseph, dated December 10, 1978, reporting a telephone conversation with counsel for one respondent:

> Mr. Savarese called to ask when I learned about the Judge's contract. I told him that I learned of it via FTC: Watch. He asked about discussions between the Judge and

[6] See footnote 7 *infra.*

me. I said that the Judge had mentioned he was considering retirement before the announcement on the record, but that we had not discussed a contract. He asked if the Judge and I had ever discussed the contract. I said no.

The others are a series of FTC staff proposed draft filings, some of which are hand-dated December 1977, that embody a projected request that Judge Hinkes make notes on the demeanor of witnesses. "Should Administrative Law Judge Hinkes, for any reason, be unable to continue presiding over the *Kellogg* hearings," the drafts state, "such preliminary notes would facilitate the transition to a successor administrative law judge * * *."

The circumstances under which complaint counsel learned of Judge Hinkes' plans to retire, and any actions taken in consequence by complaint counsel or other Bureau staff, are potentially material to our disposition of the reserved portion of General Foods' motion. The documents brought to our attention by the General Counsel may or may not be relevant, but they do require explanation.

We turn, then, to the means by which this further inquiry is to be carried out. In endeavoring to establish the facts relevant to the disposition of motions before us in the ancillary proceeding, we have twice requested affidavits from those who appeared best able to provide such facts. Order of November 13, 1979; Order of July 31, 1980. The taking of affidavits is a proper means of initial inquiry. *Grolier, Inc.* v. *FTC,* 615 F.2d 1215 (9th Cir. 1980), and cases cited in our order of July 31, 1980, at 19, note 15. Indeed, this device yielded a satisfactory evidentiary basis for our conclusion that, measuring the material facts against applicable legal standards, the relief sought by respondents as a consequence of the contract with Judge Hinkes and the negotiations preceding it was unwarranted. Order of July 31, 1980, at 14–23.

In this new phase of the inquiry, focusing on allegations of misconduct by the Bureau of Competition, the affidavits filed in compliance with our order of July 31 have likewise provided useful evidence. In particular, the affidavits set forth the discussions at the meetings of August 14 and 16, 1978, in sufficient detail so that no additional inquiry of the known participants in those events appears necessary. However, as noted earlier, the affidavits fail to establish how the Bureau of Competition learned of Judge Hinkes' intention to retire, and of course they do not account for the documents from complaint counsel's files quoted above.

While additional affidavits might resolve these matters, it is not clear to whom instructions to file such affidavits ought to be directed. Therefore, we are imposing on the Bureau of Competition itself the obligation to file, within 45 days, a report stating with

specificity, and accompanied by appropriate affidavits and documents, the date, circumstances, and content of any extrarecord conversation between Judge Hinkes and any member of the Bureau staff, presently or formerly employed, concerning Judge Hinkes' possible retirement, or of any conversation between any other law judge or any employee of the Office of Administrative Law Judges and any member of the Bureau staff, presently or formerly employed, concerning Judge Hinkes' possible retirement; and the date, circumstances, and content of any subsequent conversation among members of the Bureau staff, presently or formerly employed, concerning actions to be taken with respect to the employment or other status of Judge Hinkes, or the content of any document concerning such actions.[7]

It is impossible at this point to predict whether further factfinding will be needed after the Bureau files its report, and if so, by what precise method such factfinding ought to be accomplished. The report of the Bureau is a means by which those who know the facts may explain on the record the significance, if any, of the documents and events in question to the issues before us. If this report, together with the other evidence of record, proves to be insufficient to permit our determination of the allegations that officials of the Bureau of Competition breached the separation of functions and *ex parte* barriers in the Administrative Procedure Act and the Commission's rules, it may be necessary to seek the services of an administrative law judge from another agency to superintend such additional inquiry as will be required.

We want the facts to be produced, promptly and fully, that will enable us to sustain or reject these allegations. An ambiguity in one affidavit, and newly discovered documents that require explanation, leave us unable to find those facts after the initial round of affidavits. Aided by the views of the parties, we shall review the report and other evidence to determine whether further inquiry, under the superintendence of an outside law judge, is needed.

It is therefore ordered, That:

A. General Foods' motion to dismiss the complaint is denied, insofar as the motion is based upon allegations concerning the activities of Judge Hanscom;

B. The Bureau of Competition shall file with the Commission, within 45 days of the date of this Order, the report specified in Part II of this Order.

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[7] In addition, if it is a fact that Anthony Low Joseph attended the meeting with Messrs. Schwartz, Brickfield, Dugan, Kefauver, and Rubin on August 14, 1978 (see Rubin Aff. ¶ 5), then the Bureau's report shall be accompanied by an affidavit from Mr. Joseph, responding to the questions posed in Paragraph F of our Order of July 31.

C. Within 20 days of the filing of the report, the parties shall file their views on whether additional factfinding is necessary prior to our determination of the reserved portion of General Foods' motion, and if so, what material facts they believe need to be adduced in such additional factfinding.

D. The Secretary shall place on the docket of this proceeding, and serve upon the parties, the following documents:

(1) A memorandum to the file from Anthony Low Joseph, dated December 10, 1978; and

(2) Five drafts of proposed requests pertaining to preparation of notes on demeanor, prepared by unidentified staff members of the Bureau of Competition.

Chairman Pertschuk and Commissioner Pitofsky did not participate.

IN THE MATTER OF

SMITHKLINE CORPORATION

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT AND SEC. 7 OF THE CLAYTON ACT

Docket C-3043. Complaint, Oct. 9, 1980—Decision, Oct. 9, 1980

This consent order requires, among other things, a Philadelphia, Pa. manufacturer of prescription medicines, proprietary pharmaceuticals, and animal health products, to divest itself of the assets of Sea & Ski, except for its plant and equipment, within six months of the effective date of this order. Respondent is further required, upon request of the buyer, to furnish technical, market and quality control information for a one-year period specified in the order and to maintain the value of the products or assets of Sea & Ski and preserve it as a viable, ongoing business pending divestiture.

Appearances

For the Commission: *C. W. Corddry.*

For the respondent: *Robert Lewis, Ballard, Spahr, Andrews & Ingersoll,* Washington, D.C.

COMPLAINT

The Federal Trade Commission, having reason to believe that the above named respondent, subject to the jurisdiction of the Commission, will, on April 10, 1980, have acquired all the stock of Allergan Pharmaceuticals, Inc. in violation of Section 7 of the Clayton Act, as amended, (15 U.S.C. 18) and Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45), and having found that a proceeding in respect thereof would be in the public interest, hereby issues its complaint, pursuant to Section 11 of the Clayton Act (15 U.S.C. 21) and Section 5(b) of the Federal Trade Commission Act (15 U.S.C. 45(b)), stating its charges as follows:

I.

DEFINITION

1. For purposes of this complaint, the term "sun care products" means any formulation designed, promoted, and sold for application to the skin before or during exposure to sunlight in order to prevent, inhibit, facilitate, or simulate any condition of the skin.

II.

Respondent

2. SmithKline Corporation is a corporation organized, existing, and doing business under and by virtue of the laws of the Commonwealth of Pennsylvania with its principal office and place of business located at 1500 Spring Garden St., Philadelphia, Pennsylvania.

3. In 1979 SmithKline, including its foreign subsidiaries, had consolidated revenues of approximately $1.35 billion and consolidated assets of approximately $1.2 billion.

4. SmithKline is engaged primarily in the research, development, manufacture, and marketing of prescription medicines, proprietary pharmaceuticals, animal health products, ultrasonic and electronic instruments, cosmetics, and sun care products, and in the operation of numerous clinical laboratories.

5. SmithKline has been engaged in the manufacture and sale of sun care products through its subsidiary, the Sea & Ski Corporation, since the 1960's.

III.

The Acquired Corporation

6. Allergan Pharmaceuticals, Inc. is a corporation organized, existing, and doing business under and by virtue of the laws of the State of Delaware with its principal office and place of business at 2525 Dupont Drive, Irvine, California.

7. In 1979 Allergan, including its foreign subsidiaries, had consolidated revenues of approximately $82.45 million and consolidated assets of $88.75 million.

8. Allergan is engaged primarily in the research, development, manufacture, and marketing of prescription and non-prescription pharmaceutical products in the specialty fields of ophthalmology and dermatology.

9. Allergan, through its Herbert Laboratories division, has been engaged in the manufacture and sale of sun care products since 1974.

IV.

Jurisdiction

10. At all times relevant herein, respondent has been and is engaged in commerce within the meaning of the Clayton Act, as

amended, and engaged in or affecting commerce within the meaning of the Federal Trade Commission Act, as amended.

V.

The Acquisition

11. As of April 10, 1980, respondent SmithKline Corporation will have acquired all of the issued and outstanding shares of Allergan Pharmaceuticals, Inc. and the former shareholders of Allergan will hold approximately 4,300,000 shares of SmithKline common stock worth approximately $259 million. In this manner Allergan will become a wholly-owned subsidiary of SmithKline.

VI.

Trade and Commerce

12. For the purposes of this complaint, the relevant product market is the manufacture and sale of sun care products and the relevant geographic market is the United States.

13. Sun care products are comprised primarily of sun tanning and sun screening preparations used to control the effects on the skin of exposure to sunlight.

14. Factory sales of sun care products in the United States in 1979 are estimated to have been approximately $94 million.

15. SmithKline and Allergan have been actual competitors in the manufacture and sale of sun care products since 1974.

16. In 1979, SmithKline, through Sea & Ski, and Allergan ranked approximately fourth and seventh respectively in total sales among all sun care products manufacturers. SmithKline's share is estimated to have been approximately 8.8% and Allergan's share approximately 2.7%.

17. The sun care products market is concentrated. In 1979 the four top ranking firms accounted for approximately 70 percent of domestic sales.

18. The major manufacturers of sun care products, including respondent and Allergan Pharmaceuticals, Inc., market their products in all fifty states.

VII.

Effects of the Acquisition; Violations Charged

19. The effects of the acquisition by SmithKline of Allergan may

be substantially to lessen competition or tend to create a monopoly in the manufacture and sale of sun care products in the United States in violation of Section 7 of the Clayton Act, as amended, and Section 5 of the Federal Trade Commission Act, as amended, in the following ways, among others:

a. Actual competition between respondent and Allergan in the manufacture and sale of sun care products will be eliminated;

b. Allergan as a substantial, independent competitive factor in the manufacture and sale of sun care products will be eliminated;

c. Concentration in the manufacture and sale of sun care products will be increased, and the possibility of deconcentration may be diminished;

d. Additional acquisitions and mergers in the industry may be encouraged.

Decision and Order

The Federal Trade Commission having initiated an investigation of the proposed merger of SmithKline Corporation and Allergan Pharmaceuticals, Inc., and the respondent having been furnished thereafter with a copy of a draft of a complaint which the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission would charge respondent with violation of the Clayton and Federal Trade Commission Acts; and

The respondent and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Acts, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent SmithKline Corporation is a corporation orga-

nized, existing, and doing business under and by virtue of the laws of the Commonwealth of Pennsylvania with its office and the principal place of business located at 1500 Spring Garden St., in the City of Philadelphia, Commonwealth of Pennsylvania.

Allergan Pharmaceuticals, Inc. was a corporation organized, existing, and doing business under and by virtue of the laws of the State of Delaware with its offices and principal place of business located at 2525 Dupont Drive in the City of Irvine, State of California.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

ORDER

For the purpose of this order, the term "sun care products" means any formulation designed, promoted, and sold for application to the skin before or during exposure of sunlight in order to prevent, inhibit, facilitate, or simulate any condition of the skin.

I

It is ordered, That, subject to the prior approval of the Federal Trade Commission, respondent, through its officers, directors, employees, subsidiaries, affiliates, divisions, successors, and assigns, shall within six (6) months from the date on which this order becomes final divest absolutely and in good faith all assets, properties, rights, and privileges, tangible and intangible, of the subsidiary of respondent SmithKline Corporation known as the Sea & Ski Corporation, including but not limited to molds for the fabrication of plastic bottles, raw material reserves, inventory, lists of customers, product trade names, product trademarks, patents, assignable licenses (non-assignable licenses shall be relinquished), manufacturing specifications and procedures, market research materials, sales training materials, research and development projects (including licenses, license applications Notices of Claimed Investigational Exemption for a New Drug (IND's)), but excluding real property, plant, equipment and machinery of the Reno, Nevada, facility other than molds for the fabrication of plastic bottles. Such divestiture shall be made to a third party which represents that it intends to use the assets in the manufacture, distribution or sale of sun care products in the United States.

II

It is further ordered, That, upon the written request of the acquirer of the divested property, respondent shall, for no longer than one (1) year from the date of the agreement with such acquirer to transfer the assets referred to in Paragraph I, furnish such technical, market, and quality control information of SmithKline Corporation accumulated as a result of its ownership of the Sea & Ski Corporation and make available such personnel and technical assistance as may be necessary to enable the acquirer to manufacture and market those sun care products manufactured in the United States by SmithKline Corporation at the time of its merger with Allergan Pharmaceuticals, Inc.

III

It is further ordered, That, pending the divestiture required by this order, respondent shall not cause and shall use its best efforts to prevent, any diminution of value of the products or assets of Sea & Ski Corporation, and shall preserve the Sea & Ski Corporation as a viable, ongoing business.

IV

It is further ordered, That, pursuant to the requirements of Paragraph I above, none of the assets of the Sea & Ski Corporation shall be divested directly or indirectly to anyone who is, at the time of divestiture, an officer, director, employee, or agent of, or under the control, direction, or influence of, respondent or any of respondent's subsidiaries or affiliated corporations whether direct or indirect, or who owns or controls more than one (1) percent of the outstanding shares of the capital stock of respondent.

V

It is further ordered, That respondent shall, within sixty (60) days after the date of service of this order, and every sixty (60) days thereafter until respondent has fully complied with the divestiture provision of this order, and once thereafter on the expiration of the provisions of Paragraph II of this order, submit in writing to the Federal Trade Commission a verified report setting forth in detail the manner and form in which respondent intends to comply, is complying or has complied with this order. Until divestiture is accomplished, all compliance reports shall include, among other

336-345 O - 81 - 40

things that are from time to time required, a summary of contacts or negotiations with anyone for the disposition of the assets specified in Paragraph I of this order, the identity of all such persons and copies of all written communications between such persons and respondent.

VI

It is further ordered, That respondent notify the Federal Trade Commission at least thirty (30) days prior to any proposed change in the corporate respondent such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporation which may affect compliance obligations arising out of this order.

IN THE MATTER OF

BENTON & BOWLES, INCORPORATED

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-3044. Complaint, Oct. 10, 1980—Decision, Oct. 10, 1980

This consent order requires, among other things, a New York City advertising agency to cease depicting, in advertising, children eight years of age or younger operating non-motorized two- or three-wheeled vehicles in an unsafe or illegal manner. This includes representing children operating such vehicles in traffic thoroughfares without adult supervision, and performing stunts or similar acts which create an unreasonable risk of harm to person or property.

Appearances

For the Commission: *Susan Elliott.*

For the respondent: *Stuart Lee Friedel, Davis & Gilbert,* New York, N.Y.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that Benton & Bowles, Incorporated, a corporation, hereinafter referred to as respondent, has violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. Respondent Benton & Bowles, Incorporated is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York with its office and principal place of business located at 909 Third Ave., New York, New York.

PAR. 2. Respondent has been retained by AMF, Incorporated as its advertising agency and is now and for all times relevant to this complaint has been engaged in the production and distribution of advertisements for a variety of bicycles, tricycles and other wheeled toys manufactured by AMF, Incorporated.

PAR. 3. Respondent has prepared and placed for publication and has disseminated advertising material, including, but not limited to, the advertising referred to herein, to promote the sale of bicycles and

tricycles, including, but not limited to, the "Evel Knievel MX," the "Evel Knievel Hot Seat," and the "Avenger."

PAR. 4. In the course and conduct of its aforesaid business, respondent has been, and is now, in substantial competition in or affecting commerce with other advertising agencies.

PAR. 5. In the course and conduct of its aforesaid business, respondent has disseminated, and caused the dissemination of certain television advertisements concerning said products in or affecting commerce which were broadcast by television stations located in various States of the United States, and in the District of Columbia, having sufficient power to carry such broadcasts across state lines, for the purpose of inducing, and which were likely to induce, directly or indirectly, the purchase of said products in or affecting commerce.

PAR. 6. Typical and illustrative of the statements and representations in respondent's advertisements disseminated by means of television, but not all inclusive thereof, are the "Can't Wait" and "Avenger" advertisements. In "Can't Wait," two young boys are shown riding their respective vehicles, a bicycle and tricycle, down their parallel driveways, continuing a short distance into the adjoining street so as to greet each other, without slowing down or looking out for cars or other possible dangers to themselves or others. In "Avenger," one young boy is shown riding a bicycle on a one-way street, then turning onto a sidewalk and into a vacant dirt lot without slowing down or looking right or left, riding over rough and uneven ground in the dirt lot, and then turning into an alley without slowing down or looking right or left.

PAR. 7. A. The aforesaid advertisements have the tendency or capacity to influence young children to ride or operate a bicycle, tricycle or other similar wheeled toy in a street, road, alley or other traffic thoroughfare.

B. Furthermore, the aforesaid advertisements have the tendency or capacity to influence children to engage in the following behavior with respect to the use of bicycles, tricycles, or other similar wheeled toys:

1. Riding across rough and uneven ground on a bicycle, tricycle or other similar wheeled toy in a manner which creates an unreasonable risk of harm to person or property;

2. Riding or operating a bicycle, tricycle or other wheeled toy in a manner which is contrary to generally recognized standards of safety for the operation or use of a bicycle, tricycle or other similar wheeled toy.

Therefore, such advertisements have the tendency or capacity to induce behavior which involves an unreasonable risk of harm to person or property, and were and are therefore unfair or deceptive acts or practices.

PAR. 8. In the course and conduct of its aforesaid businesses, and at all times mentioned herein, respondent has been and is now in substantial competition, in or affecting commerce, with other corporations engaged in the advertising of bicycles, tricycles or other wheeled toys.

PAR. 9. The aforesaid acts or practices of respondent, as herein alleged as aforesaid, were and are all to the prejudice and injury of the public and of respondent's competitors, and constituted and now constitute unfair methods of competition in or affecting commerce and unfair or deceptive acts or practices in or affecting commerce, in violation of Section 5 of the Federal Trade Commission Act, as amended.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the named respondent having been furnished thereafter with a copy of a draft of complaint which the Bureau of Consumer Protection proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge the named respondent with violation of the Federal Trade Commission Act; and

The named respondent, Benton & Bowles, Incorporated, its attorneys, and counsel for the Commission having thereafter executed an agreement containing a consent order, and admission by the named respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by the named respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the named respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Sec. 2.34 of its Rules,

the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. The named respondent, Benton & Bowles, Incorporated, is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York with an office and place of business located at 909 Third Ave., New York, New York.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents, and the proceeding is in the public interest.

ORDER

For the purpose of this Order, the term "non-motorized two- or three-wheeled vehicle" shall include bicycles, tricycles, and other similar non-motorized two- or three-wheeled vehicles. The term "minibike" shall refer to motorized two-wheeled vehicles without gears and shall not include mopeds.

I.

It is ordered, That respondent Benton & Bowles, Incorporated, a corporation, hereinafter referred to as respondent, its successors and assigns, and their officers, agents, representatives, and employees, directly or through any corporation, subsidiary, division or other device, in connection with the advertising in or affecting commerce of any non-motorized two- or three-wheeled vehicle or minibike, cease and desist from, directly or by implication:

A. Representing, in any manner, any child who appears to be eight years old or younger operating any non-motorized two- or three-wheeled vehicle in any public street, road, alley or other traffic thoroughfare; *provided, however,* that this provision shall not apply to the depiction of any child who appears to be five to eight years old operating a non-motorized two- or three-wheeled vehicle in any public street, road, alley, or other traffic thoroughfare when such child is accompanied and closely supervised by a person who appears to be eighteen years old or older and who is operating a non-motorized two- or three-wheeled vehicle.

B. Representing, in any manner, any person(s) performing stunts, jumps, wheelies, or any other similar act while operating a non-motorized two- or three-wheeled vehicle when such act(s) create(s) an unreasonable risk of harm to person or property; *provided, however,* that this provision shall not apply to the depiction

of persons using motorcross bikes in an adult-supervised off-the-road setting and in which the participants are shown wearing helmets and where arms, legs, and feet are suitably covered.

C. Representing, in any manner, any person(s) operating or riding a non-motorized two- or three-wheeled vehicle in any public street, road, alley or other traffic thoroughfare:

1. without obeying all applicable official traffic control devices;
2. other than upon, astride or straddling a regular seat attached thereto;
3. with more persons on it, at any one time, than the vehicle is designed or safely equipped to carry, except that an adult rider may carry a child securely attached to its person in a back pack or sling;
4. while carrying any package, bundle, or article which obstructs vision or interferes with the proper control of the vehicle;
5. when such person attaches himself/herself or the vehicle to any other vehicle; *provided, however,* that this provision shall not apply to the depiction of a bicycle trailer or bicycle semitrailer attached to a bicycle if that trailer or semitrailer has been designed for such attachment and when the operation of such a bicycle with such an attachment does not create an unreasonable risk of harm to person or property;
6. unless such vehicle is equipped with reflectors in conformance with Section 1512.16 of the "Revised Safety Standards for Bicycles" (16 CFR 1512 (1978)) or any successor provision, rule or regulation issued by the Consumer Product Safety Commission and, in addition, a functioning headlamp whenever such person is operating or riding a non-motorized two- or three-wheeled vehicle at dawn, dusk or night;
7. while wearing loose clothing or long coats that can catch in pedals, chains or wheels;
8. against the flow of traffic;
9. unless such person exercises proper caution, such as by riding at a reasonable speed and at a reasonable distance from parked cars and the edge of the road, with respect to:

a. car doors opening and cars pulling out into traffic; and,
b. drain grates, soft shoulders and other road surface hazards;

10. in other than single file when travelling with other such vehicles; *provided, however,* that this provision shall not apply to the depiction of persons riding in other than single file when such behavior does not impede the normal and reasonable movement of

traffic and does not create an unreasonable risk of harm to person or property;

11. unless such person exercises proper caution before entering or crossing any public street, road, alley or other traffic thoroughfare from any non-traffic area by first stopping and looking right and left and yielding the right-of-way to all vehicles approaching on such public thoroughfare to the extent necessary to safely enter the flow of traffic;

12. unless such person exercises proper caution before entering or crossing any sidewalk or other pedestrian pathway by first looking right and left and yielding the right-of-way to all pedestrians approaching on such pedestrian pathway.

D. Representing, in any manner, any person operating a mini-bike in any public street, road, alley or other traffic thoroughfare, unless such operation is lawful under applicable vehicle codes.

II.

It is further ordered, That respondent shall forthwith distribute a copy of this Order to each of its operating divisions which engage or shall engage in the preparation or dissemination of advertising.

It is further ordered, That respondent notify the Commission at least thirty (30) days prior to any proposed change such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporation which may affect compliance obligations arising out of the Order.

It is further ordered, That the respondent herein shall, within sixty (60) days after service upon it of this Order, file with the Commission a report, in writing, setting forth in detail the manner and form in which it has complied with this Order.

In the Matter of

BINNEY & SMITH INC.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-3045. Complaint, Oct. 16, 1980—Decision, Oct. 16, 1980

This consent order requires, among other things, a manufacturer of art materials, located in Easton, Pa., to cease fixing the prices of its products. The firm is required to establish interest-bearing escrow accounts for the purpose of making restitution to consumers for purchases of certain school art materials. Further, the firm is required to distribute consumer redress funds to any state institutions which purchased said products; the FTC, with the cooperation of the State Attorney General, will distribute the respective funds in lump-sum amounts to each of the states which satisfy the application requirements for receiving the money.

Appearances

For the Commission: *Susan L. Belman.*

For the respondent: *Bruce A. Hecker, Shea, Gould, Climenko & Casey,* New York City.

Complaint

The Federal Trade Commission, having reason to believe that the above-named respondent has violated the Federal Trade Commission Act, and that a proceeding by it in respect thereof would be in the public interest, issues this complaint.

RESPONDENTS

1. Respondent Binney & Smith Inc. is a Delaware corporation, with its principal office located at 1100 Church Lane, Easton, Pennsylvania.

2. At all times relevant to this complaint, respondent has been engaged in the manufacture, offering for sale, sale, and distribution of chalks, crayons, watercolors, or tempera paints.

COMMERCE

3. Respondent maintains, and has maintained, a substantial course of business, including the acts and practices alleged in this complaint, in or affecting commerce, as "commerce" is defined in Section 4 of the Federal Trade Commission Act, *as amended.*

COMPETITION

4. In the course and conduct of its business, and at all times mentioned herein, respondent has been in competition with other corporations, firms, or individuals engaged in the manufacture, offering for sale, sale, and distribution of chalks, crayons, watercolors, or tempera paints, except to the extent that competition has been restrained by the acts and practices alleged in this complaint.

NATURE OF THE OFFENSE

5. In the course and conduct of its business, respondent has engaged, or is engaging, in the following acts or practices, among others:

(a) For some years from at least as early as 1972 through at least as late as 1978, respondent and competitors engaged in the manufacture and sale of chalks, crayons, watercolors, or tempera paints, met, discussed and exchanged, prior to the publication of price lists for the forthcoming year, certain prices for those products, which were to be contained in such price lists.

(b) Through the meetings, discussions, and exchanges alleged in paragraph 5(a), respondent and competitors engaged in the manufacture and sale of chalks, crayons, watercolors, or tempera paints reached understandings or agreements concerning certain prices for those products to be contained in the published price lists for the forthcoming year.

(c) From at least as early as 1972 through at least as late as 1978, respondent and competitors engaged in the manufacture and sale of chalks, crayons, watercolors, or tempera paints published and had in effect price lists which reflected a uniformity of retail prices for certain, if not all, chalks, crayons, watercolors, or tempera paints. The price lists usually were in effect for one year, and were used to establish uniform prices for sales to distributors and other customers.

(d) The price lists alleged in paragraph 5(c) reflected the understandings or agreements alleged in paragraph 5(b).

6. By means of certain, if not all, the acts and practices alleged in paragraph 5, among others, respondent, in combination, agreement, understanding, or conspiracy with others, has fixed or is fixing the prices at which certain, if not all, chalks, crayons, watercolors, or tempera paints were or are sold.

Thus, respondent has engaged, or is engaging, in unfair acts or

practices in violation of Section 5(a)(1) of the Federal Trade Commission Act.

EFFECTS

7. The capacity, tendency or effect of the above conduct of respondent was to:

(a) Fix, control, establish, stabilize, or maintain the prices at which various of respondent's chalks, crayons, watercolors, or tempera paints are sold or resold.

(b) Lessen, eliminate, frustrate or hinder actual or potential competition in the sale and distribution of various of respondent's chalks, crayons, watercolors, or tempera paints.

(c) Artificially inflate the price paid by consumers for various of respondent's chalks, crayons, watercolors, or tempera paints.

(d) Deprive consumers of prices determined by free and open competition and of the other benefits of competition.

8. The acts and practices of respondent alleged here constitute unfair acts or practices in violation of Section 5(a)(1) of the Federal Trade Commission Act.

Decision and Order

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the Cleveland Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with a violation of the Federal Trade Commission Act; and

The respondent, and its attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, dated March 17, 1980, and modified as of August 20, 1980, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in

that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, and having duly considered the comments filed thereafter by interested persons pursuant to Section 2.34 of its Rules, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. Respondent Binney & Smith Inc. is a Delaware corporation, with its principal office located at 1100 Church Lane, in the City of Easton, State of Pennsylvania.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

ORDER

As used in this order:

(a) *"Person"* means any individual, partnership, firm, corporation, association, or other business or other legal entity.

(b) *"State"* means a state, the District of Columbia, Puerto Rico, the Virgin Islands, Guam, American Samoa, the Northern Mariana Islands, and any other territory of the United States.

(c) *"State Institution"* means any state agency, instrumentality, or institution or any political subdivision thereof, including, but not limited to, any county, city, town, municipality, or school district which purchases school art materials.

(d) *"Art materials"* means any of the following products: adhesives (including art and craft glue and white paste), art kits (including combinations of crayons, watercolors, brushes, glue or chalk), brushes, chalks (including art, chalkboard and industrial chalk), craft kits (including fabric crayons and fabric crayon kits), crayons (including drawing, checking, and marking crayons), modeling clays, oil pastels, paints (including finger paint, finger paint powder, tempera, poster paint, watercolors, and transparent, powder, and textile paints), paper (including finger paint paper and stencil paper), water color markers, stencil brushes, chalkboard cleaner, stencil knives, pencils (including drawing and charcoal pencils), modeling material, excello squares, ink (including printing ink), linoleum blocks, linoleum, acrylics, and media mixer.

(e) *"Respondent"* means Binney & Smith Inc., a Delaware corporation, its subsidiaries and divisions, with its principal office located at 1100 Church Lane, Easton, Pennsylvania.

I

It is ordered, That respondent, its successors and assigns, and its officers, and respondent's agents, representatives, and employees, directly or indirectly, or through any corporation, subsidiary, division or other device, in connection with the manufacture, offering for sale, sale or distribution of art materials in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from directly or indirectly:

(1) Entering into, maintaining, or enforcing any agreement, combination, understanding or plan with any competitor to fix, determine, establish, or maintain the prices, discounts or other terms or conditions for the sale of art materials.

(2) Submitting any bid to any customer or prospective customer for the sale of any art materials when any price, term or condition of sale or any element contained in such bid was discussed with, disclosed to, or received from, directly or indirectly, any competitor, actual or potential.

(3) Circulating or sending to, or exchanging with, any other person who manufactures, distributes, markets or sells art materials, any price list, price quotation or pricing factor applicable to art materials—except for price lists, price quotations, or pricing factors provided to or received from any person in the course of, and solely related to, negotiating for, entering into, or carrying out bona fide sales or potential sales by respondent directly to such person—in advance of the printing, publication, effectuation, circulation or communication of such price lists, price quotations, or pricing factors to customers generally.

(4) Collecting from, circulating to or exchanging with, or reporting or recommending to any competitor who manufactures, distributes, markets or sells art materials, any cost factor or average cost of manufacture or sale of art materials, or any formulas for computing such cost.

(5) Communicating or exchanging with any other person who manufactures, distributes, markets, or sells art materials, any actual or proposed price, price change, discount, or other term or condition of sale at or upon which art materials are to be, or have been, sold—except for such information provided to or received from any person in the course of, and solely related to, negotiating for, entering into, or carrying out bona fide sales or potential sales by respondent directly to such person—prior to the communication of such information to customers generally.

(6) Disclosing to, or communicating to, any other person who manufactures, distributes, markets, or sells art materials:

(a) respondent's intention to submit, or not to submit, a bid to any purchaser,

(b) the fact that a bid has or has not been submitted prior to the communication of such information to the general public, or

(c) the content of any bid prior to the communication of such information to the general public; except that, in declining to furnish a price quotation to a distributor to be used in connection with a particular bid, respondent may disclose that the reason for such refusal is respondent's intention to bid directly.

II

It is further ordered, That respondent shall, for a period of five (5) years from the date of entry of this order, furnish simultaneously with each bid or quotation required to be sealed which is submitted by it for the sale of art materials to any purchaser, a written certification by an officer of respondent, that such bid was not in any way the result, directly or indirectly, of any agreement, understanding, or communication with any other producer, seller or distributor.

III

It is further ordered, That, for a period of five (5) years from the date of entry of this order, respondent shall preserve all written price computations and other written calculations actually performed by respondent in the preparation and submission of any bid required to be sealed which is submitted to any actual or potential purchaser of art materials. Respondent shall retain such written computations and calculations for a period of at least five (5) years from the date each bid which is based on such computations or calculations is submitted to any purchaser.

IV

It is further ordered, That:

(1) Respondent establish, within five (5) days after the date this order is served on respondent, an Escrow Account at the Continental Bank, 30 North LaSalle St., Chicago, Illinois, and designate Continental Bank as the Escrow Agent to receive monies, information and documents, to disburse monies and to carry out such other functions as may be provided for pursuant to the terms of this order, and the

written directions of the Federal Trade Commission or its designee. The duties of the Escrow Agent shall be as outlined in the Escrow Instructions here attached as Appendix A and incorporated herein. Further, the parties shall be bound to the terms of said Escrow Instructions whether or not they are signatories thereto.

(2) Respondent shall deposit one million dollars ($1,000,000) in the Escrow Account in the following manner. A first deposit of five hundred thousand dollars ($500,000) shall be made within five (5) days after the order is served on respondent and the second deposit of the remaining five hundred thousand dollars ($500,000) shall be made on or before February 1, 1981. In the event that the order is not served on respondent prior to February 1, 1981, the second deposit of five hundred thousand dollars ($500,000) shall be made within three (3) months after such service occurs.

(3) All interest earned on the funds deposited in the Escrow Account shall be added to the Escrow Account and disbursed by the Escrow Agent pursuant to the terms of this order, the Escrow Instructions, and the written directions of the Federal Trade Commission or its designee.

(4) Respondent shall not issue any instructions or directions respecting the Escrow Account to the Federal Trade Commission or its designee, or to the Escrow Agent with respect to the performance of their duties. These duties shall be pursuant to this order and to the Escrow Instructions, and shall include, but not be limited to, the investment of the property held by the Escrow Agent, the disbursement of the property held by the Escrow Agent, and compliance with any written directions of the Federal Trade Commission or its designee. Respondent shall not exercise any control over the property in the Escrow Account.

V

It is further ordered, That:

(1) Respondent shall submit to the Federal Trade Commission, within thirty (30) days after the date this order is served on respondent, a notarized affidavit executed by a duly authorized officer of respondent listing, to the best of its knowledge, the names of all the states within which any state institutions made purchases of respondent's chalk, crayons, watercolors, or tempera paints during any of the years 1972 through 1979, inclusive.

(2) As it has been determined by the Federal Trade Commission that the most readily identifiable and most significantly affected market consists of the school art materials purchasers, the sole

purpose of the Escrow Account established pursuant to Section IV of this order is to disburse the consumer redress funds to any state institutions that purchase chalks, crayons, watercolors, or tempera paints for schools and are located in a state listed pursuant to Section V(1) of this order. Provisions contained herein or to be adopted in the future for the distribution of the funds are and shall be designed to accomplish such purpose in a manner most feasible, efficient and not inconsistent with the other provisions of this order.

(3) The Federal Trade Commission or its designee shall determine the appropriate recipients of funds in the Escrow Account, the sum paid to each recipient, and the most appropriate method to distribute the funds, taking into consideration the amount of funds available, the administrative feasibility and costs of disbursement, and the purpose of the Escrow Account, and shall instruct the Escrow Agent to distribute the funds in accordance with its determination.

(4) Funds to be distributed pursuant to paragraphs (1) through (3) of Section V of this order shall be paid out of the Escrow Account within three (3) years after the date of service of this order. All funds remaining in the Escrow Account after three (3) years from the date of service of this order shall be returned to respondent.

VI

It is further ordered, That respondent:

(1) Serve within sixty (60) days after the entry of this order a copy of this order upon each of its officers and directors, and upon each of its employees and agents who have any responsibility for establishing prices, discounts or other terms or conditions for the sale of art materials.

(2) File with the Federal Trade Commission two (2) separate written reports setting forth in detail the manner and form in which they have complied with this order; the first report to be filed within sixty (60) days after service upon them of this order, and the second report to be filed within thirty (30) days after February 1, 1981.

(3) Notify the Commission at least thirty (30) days prior to any proposed change in the respondent which may affect compliance obligations arising out of this order.

APPENDIX A

To: Continental Illinois National Bank
and Trust Company of Chicago
Trust and Investment Service
Corporate Trust Division, Escrow Section
30 North LaSalle Street—10th Floor
Chicago, Illinois 60693

The following property will be deposited with you by the undersigned within the designated times:

Two deposits, each of Five Hundred Thousand Dollars ($500,000), for a sum total of One Million Dollars ($1,000,000), will be deposited in accordance with the instructions designated in paragraph 2 of section IV of the Agreement Containing Consent Order to Cease and Desist entered into between Binney & Smith Inc. and staff of the Cleveland Regional Office of the Federal Trade Commission, dated March 17, 1980.

As Escrowee, you are hereby directed to hold, deal with and dispose of the aforesaid property and any other property at any time held by you hereunder in the following manner subject, however, to the terms and conditions hereinafter set forth:

A. You will hold the property and any other property at any time held by you hereunder (hereinafter called the "Property") until directed in writing by the FTC or its designee to distribute the Property, in which event the Property shall be distributed in accordance with its instructions. In addition to deducting such fees, costs and expenses as incurred by you under paragraphs 7 and 8 hereof, you also will pay from the Property, as directed in writing by the FTC or its designee, such sums as you are authorized by the FTC or its designee to pay for the administration of the distribution scheme established by the FTC or its designee pursuant to the Agreement Containing Consent Order to Cease and Desist and the Decision and Order. In addition, you shall execute such contracts regarding administration and distribution of the Escrow Account as the FTC or its designee directs. Subject to this paragraph, this Escrow will terminate upon the disbursement of all the Property pursuant to the written direction of the FTC or its designee.

B. Upon receipt of the Property you will invest the proceeds in either certificates of deposit other than certificates of deposit of Escrowee, or obligations of the United States Government or its agencies, either of which will have maturity not exceeding six (6) months from date of purchase. You will invest the Property with the aim of securing principal, while maximizing interest income. In the exercise of your sound discretion, if you determine it necessary to sell any or all of the Property prior to maturity and invest the proceeds in either other certificates of deposit or obligations of the United States Government or its agencies, you may do so.

C. Upon maturity of any of the Property you will invest the proceeds in either additional certificates of deposit other than certificates of deposit of Escrowee, or obligations of the United States Government or its agencies, either of which will have maturity not exceeding six (6) months from date of purchase. You will invest the proceeds with the aim of securing principal, while maximizing interest income. In the exercise of your sound discretion, if you determine it necessary to sell any or all of the Property prior to maturity and invest the proceeds in either other certificates of deposit or obligations of the United States Government or its agencies, you may do so.

D. You will send the FTC or its designee, monthly cash and asset statements of this Escrow Account.

E. These Escrow Instructions may be amended any time by a document duly executed by the FTC or its designee entitled "Amendment to Escrow Instructions" to which you acknowledge receipt.

F. If the FTC decides to use a designee, you will not act pursuant to such designee's orders, until you receive a certified copy of the order of the FTC naming such designee.

Terms and Conditions

1. Your duties and responsibilities shall be limited to those expressly set forth in these Escrow Instructions, and you shall not be subject to, nor obliged to recognize, any other agreement between, or direction or instruction of, any or all of the parties hereto even though reference thereto may be made herein; *provided, however,* with your written consent, these Escrow Instructions may be amended at any time or times by an instrument in writing signed by the FTC or its designee.

2. You are authorized, in your sole discretion, to disregard any and all notices or instructions given by any of the undersigned or by any other person, firm or corporation, except only such notices or instructions as are hereinabove provided for and orders or process of any court entered or issued with or without jurisdiction. If any Property subject hereto is at any time attached, garnished, or levied upon under any court order or in case the payment, assignment, transfer, conveyance or delivery of any such Property shall be stayed or enjoined by any court order, or in case any order, judgment or decree shall be made or entered by any court affecting such Property or any part thereof, then and in any of such events you are authorized, in your sole discretion, to rely upon and comply with any such order, writ, judgment or decree which you are advised by legal counsel of your own choosing is binding upon you; and if you comply with any such order, writ, judgment or decree you shall not be liable to any of the parties hereto or to any other person, firm or corporation by reason of such compliance even though such order, writ, judgment or decree may be subsequently reversed, modified, annulled, set aside or vacated.

3. You shall not be personally liable for any act taken or omitted hereunder if taken or omitted by you in good faith and in the exercise of your own best judgment. You shall also be fully protected in relying upon any written notice, demand, certificate or document which you in good faith believe to be genuine.

4. Unless otherwise specifically indicated herein you shall proceed as soon as practicable to collect any checks or other collection items at any time deposited hereunder. All such collection shall be subject to the usual collection agreement regarding items received by your commercial banking department for deposit or collection. You shall not be required or have a duty to notify anyone of any payment or maturity under the terms of any instrument deposited hereunder, nor to take any legal action to enforcement payment of any check, note or security deposited hereunder. You shall have no liability to pay interest on any money deposited or received hereunder.

5. You shall not be responsible for the sufficiency or accuracy of the form, execution, validity or genuineness of documents or securities now or hereafter deposited hereunder, or of any endorsement thereon, or for any lack of endorsement thereon, or for any description therein, nor shall you be responsible or liable in any respect on account of the identity, authority or rights of the persons executing or delivering or purporting to execute or deliver any such document, security or endorsement or these Escrow Instructions.

6. Any notices which you are required or desire to give hereunder to the FTC or its designee shall be in writing and may be given by mailing the same to the address provided by the FTC or its designee, by United States mail, postage prepaid. For all

purposes hereof any notice so mailed shall be as effectual as though served upon the FTC or its designee to whom it was mailed at the time it is deposited in the United States mail by you whether or not the FTC or its designee thereafter actually receives such notice. Notices to you shall be in writing and shall not be deemed to be given until actually received by your trust department employee or officer who administers this Escrow. Whenever under the terms hereof the time for giving a notice or performing an act falls upon a Saturday, Sunday, or holiday, such time shall be extended to the next business day.

7. If you believe it to be reasonably necessary to consult with counsel concerning any of your duties in connection with this Escrow, or in case you become involved in litigation on account of being Escrowee hereunder or on account of having received Property subject hereto, then in either case, your costs, expenses, and reasonable attorney's fees shall be paid by you from the Property with the approval of the FTC or its designee.

8. You shall be paid a reasonable fee for your services and reimbursed for your costs and expenses hereunder by you from the Property in accordance with the fee schedule attached hereto as Appendix 1 and incorporated herein.

9. If your fees, costs, expenses, or reasonable attorney's fees provided for herein, are not promptly paid, you shall have the right to sell the Property held hereunder and reimburse yourself therefor from the proceeds of such sale or from the cash held hereunder.

10. It is understood that you reserve the right to resign as Escrowee at any time by giving written notice of your resignation, specifying the effective date thereof, to the FTC or its designee. Within 30 days after receiving the aforesaid notice, the FTC or its designee agrees to appoint a successor Escrowee to which you may distribute the Property then held hereunder, less your fees, costs and expenses. If a successor Escrowee has not been appointed and has not accepted such appointment by the end of the 30-day period, you may apply to a court of competent jurisdiction for the appointment of a successor Escrowee, and the costs, expenses and reasonable attorneys' fees which you incur in connection with such a proceeding shall be paid from the Property.

11. The Escrowee will have no liability if, in order to make the distribution, there is any loss of interest resulting from the liquidation of investments prior to their maturity.

12. The Escrowee shall have no responsibility for any taxes arising with regard to the Escrow Account. Such tax obligation, if any, shall be the responsibility of the recipients of the Property.

13. This Escrow Agreement shall be construed, enforced, and administered in accordance with the laws of the State of Illinois.

14. The undersigned Escrowee hereby agrees to hold, deal with and dispose of said Property and other Property at any time held by it hereunder in accordance with the foregoing Escrow Agreement.

15. Executed this _____ day of _____, _____ at Chicago, Illinois.

Parties to Escrow	Addresses
_____	_____
_____	_____
_____	_____
_____	_____
_____	_____
_____	_____

ATTEST: Continental Illinois National Bank and Trust Company of Chicago, Escrowee

Trust Officer By: Vice President

Executed in _____ Copies

Appendix 1

SCHEDULE OF FEES FOR SERVICES AS ESCROW AGENT

A. ADMINISTRATION FEES

The following rates are applicable for ordinary services in handling an escrow subject to a minimum acceptance fee of $250 and minimum annual charge of $250. The Acceptance Fee will be based on the initial value of the deposits at the opening of the account.

ACCEPTANCE FEE

$250 minimum on assets up to $50,000
$1.25 per $1,000 on next $300,000 valuation
$ .50 per $1,000 on next $350,000 valuation
$ .20 per $1,000 on next $1,000,000 valuation
$ .10 per $1,000 on excess above $1,700,000 valuation

ANNUAL ADMINISTRATIVE FEE

$250 minimum on assets up to $50,000
$1.25 per $1,000 on next $300,000 valuation
$ .50 per $1,000 on next $350,000 valuation
$ .20 per $1,000 on next $1,000,000 valuation
$ .10 per $1,000 on excess above $1,700,000 valuation

The Annual Administrative Fee will be based on the value of the assets in the account at the beginning of the fee period plus any deposits made through the fee billing period.

When our only current duties consist of holding life or casualty insurance policies, the minimum annual fee will be reduced to $150 until the occurrence of a casualty, at which time the regular schedule will apply to the insurance proceeds.

* * * * * * *

B. OPERATING SERVICE FEES

When the escrow account requires the maintenance of participants' or claimants'

records, the issuance of payments, and the preparation of tax forms, the following schedule applies:

1.) $2.50 per account per year (includes up to two distributions),
2.) $0.50 per check issued over two distributions.

When the escrow requires the investment of funds, a $50 charge will be made for each purchase or sale transaction. A $35 charge will be made for any free deposit or delivery of assets (securities, deeds, insurance policies, etc.).

C. TERMINATION

There are no separate termination charges. Fees for the final billing period will be prorated to the date of termination; subject to a minimum of six months from the date of inception.

D. MISCELLANEOUS

The fees quoted in this schedule apply to services ordinarily rendered in administering an escrow account, and are subject to a reasonable adjustment if we are called upon to undertake unusual duties, responsibilities, procedures, or if the cost of doing business increases. The cost of all stationery and supplies, telephone, postage, printing, or other out-of-pocket expenses will be added to our regular service charges.

In determining our general schedule of fees, we have taken into consideration the various incidental benefits occurring to us from the operation of accounts. These include temporary availability to the Trust Department of funds resulting from the retention of dividends or interest in accounts pending disbursement, the execution of securities transactions for accounts, and funds from other sources.

* * * * * * *

IN THE MATTER OF

MILTON BRADLEY COMPANY

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-3046. Complaint, Oct. 16, 1980—Decision, Oct. 16, 1980

This consent order requires, among other things, a manufacturer of art materials, located in Springfield, Mass., to cease fixing the prices of its products. The firm is required to establish interest-bearing escrow accounts for the purpose of making restitution to consumers for purchases of certain school art materials. Further, the firm is required to distribute consumer redress funds to any state institutions which purchased said products; the FTC, with the cooperation of the State Attorney General, will distribute the respective funds in lump-sum amounts to each of the states which satisfy the application requirements for receiving the money.

Appearances

For the Commission: *Susan L. Belman.*

For the respondent: *Richard G. Schultz, Foran, Wiss & Schultz,* Chicago, Ill.

COMPLAINT

The Federal Trade Commission, having reason to believe that the above-named respondent has violated the Federal Trade Commission Act, and that a proceeding by it in respect thereof would be in the public interest issues this complaint.

RESPONDENT

1. Respondent Milton Bradley Company is a Massachusetts corporation, with its principal office located at 1500 Main St., Springfield, Massachusetts.

2. At all times relevant to this complaint, respondent has been engaged in the manufacture, offering for sale, sale, and distribution of chalks, crayons, watercolors or tempera paints.

COMMERCE

3. Respondent has maintained a substantial course of business, including the acts and practices alleged in this complaint, in or affecting commerce, as "commerce" is defined in Section 4 of the Federal Trade Commission Act, as amended.

COMPETITION

4. In the course and conduct of its business, and at all times mentioned herein, respondent has been in competition with other corporations, firms, or individuals engaged in the manufacture, offering for sale, sale and distribution of chalks, crayons, watercolors or tempera paints, except to the extent that competition has been restrained by the acts and practices alleged in this complaint.

NATURE OF THE OFFENSE

5. In the course and conduct of its business, for some years continuing into 1976, respondent and other manufacturers of chalks, crayons, watercolors or tempera paints, communicated with each other prices which were to be contained in proposed price lists for those products, and entered into a horizontal agreement, conspiracy, planned common course of action, or series of horizontal arrangements to fix, stabilize, maintain, or tamper with the manufacturers' price structure of chalks, crayons, watercolors or tempera paints at the primary level of distribution.

Thus, respondent has engaged in unfair acts or practices in violation of Section 5(a)(1) of the Federal Trade Commission Act.

EFFECTS

6. The capacity, tendency or effect of the above conduct of respondent was to:

(a) Fix, control, establish or maintain the prices at which various of respondent's chalks, crayons, watercolors or tempera paints are sold.

(b) Artificially inflate the price paid by consumers for various of respondent's chalks, crayons, watercolors or tempera paints.

(c) Deprive consumers of prices determined by free and open competition and of the other benefits of competition.

7. The acts and practices of respondent alleged here constitute unfair acts or practices in violation of Section 5(a)(1) of the Federal Trade Commission Act.

Decision and Order

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a

copy of a draft of complaint which the Cleveland Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with a violation of the Federal Trade Commission Act; and

The respondent, and its attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, dated January 25, 1980, and modified as of August 18, 1980, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, and having duly considered the comments filed thereafter by interested persons pursuant to Section 2.34 of its Rules, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. Respondent Milton Bradley Company is a Massachusetts corporation, with its principal office located at 1500 Main St., in the City of Springfield, State of Massachusetts.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

ORDER

As used in this order:

(a) "*Person*" means any individual, partnership, firm, corporation, association, business or other legal entity.

(b) "*State*" means a state, the District of Columbia, Puerto Rico, the Virgin Islands, Guam, American Samoa, the Northern Mariana Islands, and any other territory of the United States.

(c) "*State Institution*" means any state agency, instrumentality, or institution or any political subdivision thereof, including, but not limited to, any county, city, town, municipality, or school district.

(d) "*Art materials*" means any of the following products: adhesives

(including art and craft glue and white paste), brushes, chalks (including art, chalkboard and industrial chalk), crayons (including drawing, checking, and marking crayons), modeling clays, oil pastels, paints (including finger paint, finger paint powder, tempera, poster paint, watercolors, and transparent, powder, and textile paints), watercolor markers, stencil brushes, chalkboard cleaner, stencil knives, modeling material, excello squares, ink (including printing ink), linoleum blocks, linoleum, media mixer, acrylics, and paper trimmers.

(e) *"Respondent"* means the Milton Bradley Company, a Massachusetts corporation, its subsidiaries and divisions, with its principal office located at 1500 Main St., Springfield, Massachusetts 01115.

I

It is ordered, That respondent, its successors and assigns, and its officers, and respondent's agents, representatives, and employees, directly or indirectly, or through any corporation, subsidiary, division or other device, in connection with the manufacture, offering for sale, sale or distribution of art materials in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from directly or indirectly:

(1) Entering into, maintaining, or enforcing any agreement, combination, understanding or plan with any competitor to fix, determine, establish, or maintain the prices, discounts or other terms or conditions for the sale of art materials.

(2) Submitting any bid to any customer or prospective customer for the sale of any art materials when any price, term or condition of sale or any element contained in such bid was discussed with, disclosed to, or received from, directly or indirectly, any competitor, actual or potential.

(3) Circulating or sending to, or exchanging with, any other person who manufactures, distributes, markets or sells art materials, any price list, price quotation or pricing factor applicable to art materials—except for price lists, price quotations, or pricing factors provided to or received from any person in the course of, and solely related to, negotiating for, entering into, or carrying out bona fide sales or potential sales by respondent directly to such person—in advance of the printing, publication, effectuation, circulation or communication of such price lists, price quotations, or pricing factors to customers generally.

(4) Communicating or exchanging with any other person who manufactures, distributes, markets, or sells art materials, any actual

or proposed price, price change, discount, or other term or condition of sale at or upon which art materials are to be, or have been, sold—except for such information provided to or received from any person in the course of, and solely related to, negotiating for, entering into, or carrying out bona fide sales or potential sales by respondent directly to such person—prior to the communication of such information to customers generally.

(5) Disclosing to, or communicating to, any other person who manufactures, distributes, markets, or sells art materials:

(a) respondent's intention to submit, or not to submit, a bid to any purchaser,

(b) the fact that a bid has or has not been submitted prior to the communication of such information to the general public, or

(c) the content of any bid prior to the communication of such information to the general public;

except that, in declining to furnish a price quotation to a distributor to be used in connection with a particular bid, respondent may disclose that the reason for such refusal is respondent's intention to bid directly.

Nothing in Section I shall be construed to prevent New England School Supply, a division of Milton Bradley Company, from carrying out its ordinary, lawful course of business, which business is limited to the secondary level of distribution and includes the purchasing of art materials and other educational products from Milton Bradley Company, Milton Bradley's competitors, and others, and the resale and distribution of such materials to the school and commercial markets. However, respondent shall not use New England School Supply, nor any distributor, as an instrument or medium to achieve, accomplish, promote or engage in any of the acts or practices described in the paragraphs (1) through (5) of Section I or in any way to circumvent the prohibitions contained in Section I of this order, all of which prohibitions are intended to address conduct between horizontal competitors.

II

It is further ordered, That, for a period of five (5) years from the date of entry of this order, respondent shall preserve all written price computations and other written calculations actually performed by respondent in the preparation and submission of any bid required to be sealed which is submitted to any actual or potential

purchaser of art materials. Respondent shall retain such written computations and calculations for a period of at least five (5) years from the date each bid which is based on such computations or calculations is submitted to any purchaser.

Section II of this order shall not apply to New England School Supply, a division of the Milton Bradley Company, in New England School Supply's ordinary, lawful course of business, which business is limited to the secondary level of distribution and includes the purchasing of art materials and other educational products from Milton Bradley Company, Milton Bradley's competitors, and others, and the resale and distribution of such materials to the school and commercial markets.

III

It is further ordered, That respondent shall not issue any instructions or directions respecting the Escrow Account to the Federal Trade Commission or its designee, or to the Escrow Agent, with respect to the performance of their duties. These duties shall be pursuant to this order and to the Escrow Instructions, and shall include, but not be limited to, the investment of the property held by the Escrow Agent, the disbursement of the property held by the Escrow Agent, and compliance with any written directions of the Federal Trade Commission or its designee. Respondent shall not exercise any control over the property in the Escrow Account.

IV

It is further ordered, That:

(1) Respondent shall submit to the Federal Trade Commission, within thirty (30) days after the date this order is served on respondent, a notarized affidavit executed by a duly authorized officer of respondent listing, to the best of its knowledge, the names of all the states within which any state institutions made purchases of respondent's chalks, crayons, watercolors or tempera paints during any of the years 1972 through 1976, inclusive.

(2) As it has been determined by the Federal Trade Commission that the most readily identifiable and most significantly affected market consists of the school art materials purchasers, the purpose of the Escrow Account established pursuant to agreement paragraphs 8, 9, 10, 11 and Section III of this order is to disburse the consumer redress funds to any state institutions that purchase

chalks, crayons, watercolors or tempera paints for schools and are located in a state listed pursuant to Section IV(1) of this order.

(3) The Federal Trade Commission or its designee shall determine the appropriate recipients of funds in the Escrow Account, the sum paid to each recipient, and the most appropriate method to distribute the funds, taking into consideration the amount of funds available, the administrative feasibility and costs of disbursement, and the purposes of the Escrow Account, and shall instruct the Escrow Agent to distribute the funds in accordance with its determination.

(4) Funds to be distributed pursuant to Section IV of this order shall be paid out of the Escrow Account within three (3) years after the date of service of this order.

V

It is further ordered, That respondent:

(1) Serve within sixty (60) days after the date this order becomes final, a copy of this order upon each of its officers and directors, and upon each of its employees and agents who have any responsibility for establishing prices, discounts or other terms or conditions for the sale of art materials.

(2) Within sixty (60) days after service upon them of this order, file with the Federal Trade Commission a report, in writing, setting forth in detail the manner and form in which they have complied with this order.

(3) Notify the Commission at least thirty (30) days prior to any proposed change in the respondent which may affect compliance obligations arising out of this order.

Appendix A

To: Continental Illinois National Bank
and Trust Company of Chicago
Trust and Investment Services
Corporate Trust Division, Escrow Section
30 North LaSalle Street—10th Floor
Chicago, Illinois 50593

The following property is deposited with you by the undersigned:

Two Hundred Thousand Dollars ($200,000)

As Escrowee, you are hereby directed to hold, deal with and dispose of the aforesaid property and any other property at any time held by you hereunder in the following manner subject, however, to the terms and conditions hereinafter set forth:

A. In the event you are notified in writing by the Federal Trade Commission (hereinafter called the "FTC") or its designee that it has accepted the Agreement Containing Consent Order to Cease and Desist entered into between Milton Bradley Company (hereinafter called the "Company") and the staff of the Cleveland Regional Office of the Federal Trade Commission, dated January 25 , 1980, and that the FTC has issued a Decision and Order in the Matter of Milton Bradley Company, a corporation, you will hold the property and any other property at any time held by you hereunder (hereinafter called the "Property") until directed in writing by the FTC or its designee to distribute the Property, in which event the Property shall be distributed in accordance with its instructions. In addition to deducting such fees, costs and expenses as incurred by you under paragraphs 7 and 8 hereof, you also will pay from the Property, as directed in writing by the FTC or its designee, such sums as you are authorized by the FTC or its designee to pay for the administration of the distribution scheme established by the FTC or its designee pursuant to the Agreement Containing Consent Order to Cease and Desist and the Decision and Order. In addition, you shall execute such contracts regarding administration and distribution of the Escrow Account as the FTC or its designee directs. Subject to this paragraph, this Escrow will terminate upon the disbursement of all the Property pursuant to the written direction of the FTC or its designee.

B. In the event the FTC or its designee notifies you that it has determined not to accept the Agreement Containing Consent Order to Cease and Desist and to issue a Decision and Order as provided in Paragraph A, this Escrow will terminate and the Property will be returned by you to the Company not later than ten days after receipt of written notice from the FTC or its designee that the Agreement was not accepted.

C. Upon receipt of the Property you will invest the proceeds in either certificates of deposit other than certificates of deposit of Escrowee, or obligations of the United States Government or its agencies, either of which will have maturity not exceeding six (6) months from date of purchase. You will invest the Property with the aim of securing principal, while maximizing interest income. In the exercise of your sound discretion, if you determine it necessary to sell any or all of the Property prior to maturity and invest the proceeds in either other certificates of deposit or obligations of the United States Government or its agencies, you may do so.

D. Upon maturity of any of the Property you will invest the proceeds in either additional certificates of deposit other than certificates of deposit of Escrowee, or obligations of the United States Government or its agencies, either of which will have maturity not exceeding six (6) months from date of purchase. You will invest the proceeds with the aim of securing principal, while maximizing interest income. In the exercise of your sound discretion, if you determine it necessary to sell any or all of the Property prior to maturity and invest the proceeds in either other certificates of deposit or obligations of the United States Government or its agencies, you may do so.

E. You will send the FTC or its designee, monthly cash and asset statements of this Escrow Account.

F. These Escrow instructions may be amended any time by a document duly executed by the FTC or its designee entitled "Amendment to Escrow Instructions" to which you acknowledge receipt.

G. If the FTC decides to use a designee, you will not act pursuant to such designee's orders, until you receive a certified copy of the order of the FTC naming such designee.

Terms and Conditions

1. Your duties and responsibilities shall be limited to those expressly set forth in these Escrow Instructions, and you shall not be subject to, nor obliged to recognize, any other agreement between, or direction or instruction of, any or all of the parties hereto even though reference thereto may be made herein; *provided, however,* with your written consent, these Escrow Instructions may be amended at any time or times by an instrument in writing signed by the FTC or its designee.

2. You are authorized, in your sole discretion, to disregard any and all notices or instructions given by any of the undersigned or by any other person, firm or corporation, except only such notices or instructions as are hereinabove provided for and orders or process of any court entered or issued with or without jurisdiction. If any Property subject hereto is at any time attached, garnished, or levied upon under any court order or in case the payment, assignment, transfer, conveyance or delivery of any such Property shall be stayed or enjoined by any court order, or in case any order, judgment or decree shall be made or entered by any court affecting such Property or any part thereof, then and in any of such events you are authorized, in your sole discretion, to rely upon and comply with any such order, writ, judgment or decree which you are advised by legal counsel of your own choosing is binding upon you; and if you comply with any such order, writ, judgment or decree you shall not be liable to any of the parties hereto or to any other person, firm or corporation by reason of such compliance even though such order, writ, judgment or decree may be subsequently reversed, modified, annulled, set aside or vacated.

3. You shall not be personally liable for any act taken or omitted hereunder if taken or omitted by you in good faith and in the exercise of your own best judgment. You shall also be fully protected in relying upon any written notice, demand, certificate or document which you in good faith believe to be genuine.

4. Unless otherwise specifically indicated herein you shall proceed as soon as practicable to collect any checks or other collection items at any time deposited hereunder. All such collection shall be subject to the usual collection agreement regarding items received by your commercial banking department for deposit or collection. You shall not be required or have a duty to notify anyone of any payment or maturity under the terms of any instrument deposited hereunder, nor to take any legal action to enforce payment of any check, note or security deposited hereunder. You shall have no liability to pay interest on any money deposited or received hereunder.

5. You shall not be responsible for the sufficiency or accuracy of the form, execution, validity or genuineness of documents or securities now or hereafter deposited hereunder, or of any endorsement thereon, or for any lack of endorsement thereon, or for any description therein, nor shall you be responsible or liable in any respect on account of the identity, authority or rights of the persons executing or delivering or purporting to execute or deliver any such document, security or endorsement or these Escrow Instructions.

6. Any notices which you are required or desire to give hereunder to the FTC or its designee shall be in writing and may be given by mailing the same to the address provided by the FTC or its designee by United States mail, postage prepaid. For all purposes hereof any notice so mailed shall be as effectual as though served upon the FTC or its designee to whom it was mailed at the time it is deposited in the United States mail by you whether or not the FTC or its designee thereafter actually receives such notice. Notices to you shall be in writing and shall not be deemed to be given until actually received by your trust department employee or officer who administers this Escrow. Whenever under the terms hereof the time for giving a notice or

performing an act falls upon a Saturday, Sunday, or holiday, such time shall be extended to the next business day.

7. If you believe it to be reasonably necessary to consult with counsel concerning any of your duties in connection with this Escrow, or in case you become involved in litigation on account of being Escrowee hereunder or on account of having received Property subject hereto, then in either case, your costs, expenses, and reasonable attorney's fees shall be paid by you from the Property with the approval of the FTC or its designee.

8. You shall be paid a reasonable fee for your services and reimbursed for your costs and expenses hereunder by you from the Property in accordance with the fee schedule attached hereto as Appendices 1 and 2 and incorporated herein.

9. If your fees, costs, expenses, or reasonable attorney's fees provided for herein, are not promptly paid, you shall have the right to sell the Property held hereunder and reimburse yourself therefor from the proceeds of such sale or from the cash held hereunder.

10. It is understood that you reserve the right to resign as Escrowee at any time by giving written notice of your resignation, specifying the effective date thereof, to the FTC or its designee. Within 30 days after receiving the aforesaid notice, the FTC or its designee agrees to appoint a successor Escrowee to which you may distribute the Property then held hereunder, less your fees, costs and expenses. If a successor Escrowee has not been appointed and has not accepted such appointment by the end of the 30-day period, you may apply to a court of competent jurisdiction for the appointment of a successor Escrowee, and the costs, expenses and reasonable attorneys' fees which you incur in connection with such a proceeding shall be paid from the Property.

11. The Escrowee will have no liability if, in order to make the distribution, there is any loss of interest resulting from the liquidation of investments prior to their maturity.

12. The Escrowee shall have no responsibility for any taxes arising with regard to the Escrow Account. Such tax obligation, if any, shall be the responsibility of the recipients of the Property.

13. The only financial responsibility or liability of the Company with regard to the Escrow Account shall be its obligation to make the timely payment of Two Hundred Thousand Dollars ($200,000) to the Escrow Account.

14. This Escrow Agreement shall be construed, enforced, and administered in accordance with the laws of the State of Illinois.

15. The undersigned Escrowee hereby acknowledges receipt of the Property described in the above Escrow Agreement and agrees to hold, deal with and dispose of said Property and other Property at any time held by it hereunder in accordance with the foregoing Escrow Agreement.

16. Executed this _____ day of _____, _____ at Chicago, Illinois.

Parties to Escrow	Addresses
_____	_____
_____	_____
_____	_____
_____	_____
_____	_____
_____	_____
_____	_____

_____

ATTEST: Continental Illinois National Bank and Trust Company of Chicago, Escrowee

_____ By: _____

Trust Officer Vice President

Executed in ____ Copies

APPENDIX 1

SCHEDULE OF FEES FOR SERVICES AS ESCROW AGENT

A. ADMINISTRATION FEES

The following rates are applicable for ordinary services in handling an escrow subject to a minimum acceptance fee of $250 and minimum annual charge of $250. The Acceptance Fee will be based on the initial value of the deposits at the opening of the account.

ACCEPTANCE FEE

$250 minimum on assets up to $50,000
$1.25 per $1,000 on next $300,000 valuation
$ .50 per $1,000 on next $350,000 valuation
$ .20 per $1,000 on next $1,000,000 valuation
$ .10 per $1,000 on excess above $1,700,000 valuation

ANNUAL ADMINISTRATIVE FEE

$250 minimum on assets up to $50,000
$1.25 per $1,000 on next $300,000 valuation
$ .50 per $1,000 on next $350,000 valuation
$ .20 per $1,000 on next $1,000,000 valuation
$ .10 per $1,000 on excess above $1,700,000 valuation

The Annual Administrative Fee will be based on the value of the assets in the account at the beginning of the fee period plus any deposits made through the fee billing period.

When our only current duties consist of holding life or casualty insurance policies, the minimum annual fee will be reduced to $150 until the occurrence of a casualty, at which time the regular schedule will apply to the insurance proceeds.

* * * * * * *

APPENDIX 2

B. OPERATING SERVICE FEES

When the escrow account requires the maintenance of participants' or claimants'

records, the issuance of payments, and the preparation of tax forms, the following schedule applies:

1.) $2.50 per account per year (includes up to two distributions),
2.) $0.50 per check issued over two distributions.

When the escrow requires the investment of funds, a $50 charge will be made for each purchase or sale transaction. A $35 charge will be made for any free deposit or delivery of assets (securities, deeds, insurance policies, etc.).

C. TERMINATION

There are no separate termination charges. Fees for the final billing period will be prorated to the date of termination; subject to a minimum of six months from the date of inception.

D. MISCELLANEOUS

The fees quoted in this schedule apply to services ordinarily rendered in administering an escrow account, and are subject to a reasonable adjustment if we are called upon to undertake unusual duties, responsibilities, procedures, or if the cost of doing business increases. The cost of all stationery and supplies, telephone, postage, printing, or other out-of-pocket expenses will be added to our regular service charges.

In determining our general schedule of fees, we have taken into consideration the various incidental benefits occurring to us from the operation of accounts. These include temporary availability to the Trust Department of funds resulting from the retention of dividends or interest in accounts pending disbursement, the execution of securities transactions for accounts, and funds from other sources.

* * * * * * *

336-345 O - 81 - 42

IN THE MATTER OF

E. I. DUPONT DE NEMOURS & COMPANY

Docket 9108. Interlocutory Order, Oct. 20, 1980

ORDER INVITING ADDITIONAL BRIEFS ON RESPONDENT'S MOTION FOR CONTINUED *IN CAMERA* TREATMENT

By motion filed January 16, 1980, respondent E. I. DuPont de Nemours and Company ("DuPont") requested a three year extension of *in camera* protection for certain documents in the record in this case. Administrative Law Judge Miles J. Brown previously ordered that these materials be given *in camera* treatment until the date of the Commission's final order or as otherwise ordered by the Commission. As indicated in DuPont's motion and confirmed in a subsequent pleading, complaint counsel have no objection to a three year extension of *in camera* treatment except to the extent that the Commission finds it necessary to refer to *in camera* evidence in its opinion. In a supplemental memorandum, DuPont raised additional issues concerning the effect of the Federal Trade Commission Improvement Act of 1980, Pub. Law 96-252, on our adjudicative *in camera* standards. Complaint counsel did not address respondent's contention that the legislation modified the criteria for *in camera* treatment because they do not oppose the requested extension.

We reject respondent's supplemental arguments at the outset and state our view that the provisions of the Improvement Act governing treatment of confidential information do not apply to or affect the Commission's standards for *in camera* protection of exhibits in adjudicative proceedings. Those standards are clearly expressed in *H.P. Hood & Sons, Inc.*, 58 F.T.C. 1184 (1961); *Bristol-Myers Company*, 90 F.T.C. 455 (1977); and *General Foods Corporation*, Dkt. 9085, Order of March 10, 1980.

In applying the standards set forth in these cases to the instant motion for extended *in camera* treatment, we have found that certain issues raised by the respondent require clarification before a final determination can be made. While some of the documents appear to warrant extended *in camera* protection, the appropriate treatment for other data is less clear. Accordingly, we invite respondent, and complaint counsel should they so desire, to submit additional briefs on the following matters:

(1) Respondent has argued that certain earnings data should be given *in camera* treatment not only because of their commercial sensitivity, but also because a ruling by the Internal Revenue

Service that "disclosure of non-LIFO basis financial information in this proceeding does not constitute a violation of the LIFO conformity requirements of the Code" was apparently conditioned on such data remaining *in camera.* We are unconvinced, as yet, that the respondent's argument concerning the IRS ruling affords a satisfactory basis to grant continued *in camera* protection. While increased tax liability following the release of the earnings data might well be something that DuPont legitimately desires to avoid, the *in camera* standards enunciated in *H.P. Hood* and its progeny require us to focus on the likelihood of injury to a company's *commercial* or *competitive* position. In addition to addressing the issue of the continued commercial importance of these data, DuPont should also address further the effect of removing *in camera* protection on the IRS' ruling and the applicability of the *Hood* standard to the kind of injury asserted here.

(2) Exhibits CX 129C, 173B, 173D, 178T, 182G, 182H, 182I, and 182J are entitled to *in camera* treatment, according to DuPont, because they contain recent and highly sensitive business information. The data contained in these documents—generally profits, earnings, unit costs, and sales volumes for titanium dioxide—do appear to comprise information that, if recent, would normally be viewed as highly sensitive. However, the data here concern the years 1973 through 1976, with estimates covering years no more recent than 1977. DuPont should explain more fully how the release of this information would result in serious injury to its competitive or commercial position today.

We also note that some of this information already may have been publicly released. For example, CX 133N reveals DuPont's actual return on investment in titanium dioxide as of 1976, and CX 26I projects sales volumes, investment volumes, earnings, and returns on investment for titanium dioxide for 1972–1984. In *Bristol-Myers Company, supra,* the Commission stated that "demonstrating serious injury requires the applicant to show that the documents [to be protected] are secret . . . ." 90 F.T.C. 455, 456. DuPont has not satisfactorily addressed the impact that prior disclosures have had on the likelihood that serious competitive injury would result from the release of exhibits CX 129C, 173B, 173D, 178T, 182G, 182H, 182I, and 182J.

(3) Information contained in exhibits CX 81E, 81F, 82, 83, and 98C similarly appears to have been disclosed or so closely resembles information previously disclosed in the record that it may no longer be commercially sensitive or secret. Specifically, CX 28E, apparently prepared in 1972, shows the unit costs of titanium dioxide production

by plant for both DuPont and its competitors, as well as sales prices and operative earnings. CX 26M, also prepared in 1972, reveals costs, operative earnings, return on investment and total investment for DuPont's plants. Exhibits CX 81E, 81F, 82, 83, and 98C evidently contain the same types of information for the years 1973 and 1975. In its additional briefs, DuPont should discuss any material differences between the information in these five exhibits and data that have already been disclosed.

(4) DuPont further asserts that another group of documents contains sensitive financial information from its departmental quarterly reports, the release of which would give its competitors an injurious insight into its strengths and weaknesses. However, among these documents we notice several bare listings of selling prices of titanium dioxide by month for 1976 and 1977, indexed to a base year. These are exhibits RX 35K, RX 36J, RX 37L, RX 38L, RX 39L, and RX 40M. The age and apparent public nature of this information suggest that the exhibits need not be given extended *in camera* protection. We therefore request that DuPont explain why the release of these data would be likely to result in serious injury to its competitive or commercial position. Accordingly,

It is ordered, That the respondent and complaint counsel be given thirty days from the date of issuance of this order in which to submit briefs discussing the issues noted above. *In camera* protection of the exhibits that are the subject of respondent's motion shall be extended until the Commission issues an order disposing of that motion.

IN THE MATTER OF

E. I. DUPONT DE NEMOURS & COMPANY

FINAL ORDER, OPINION, ETC., IN REGARD TO ALLEGED VIOLATION OF SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT

Docket 9108. Complaint, April 5, 1978—Order, Oct. 20, 1980

This order sustains the initial decision of the administrative law judge and dismisses the complaint issued April 5, 1978 charging a Wilmington, Del. chemical manufacturer with attempting to monopolize the domestic titanium dioxide market. The Commission holds that since the conduct of the company was "consistent with its own technological capacity and market opportunities," it was "reasonable" and not a violation of law.

Appearances

For the Commission: *James C. Egan, Jr.* and *Robert W. Doyle, Jr.*

For the respondent: *William E. Kirk, Jr.* and *Howard J. Rudge,* Wilmington, Del. and *Daniel M. Gribbon, Covington & Burling,*[1] Washington, D.C.

COMPLAINT

The Federal Trade Commission, having reason to believe that E. I. DuPont de Nemours & Company has violated and is now violating Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45, and that a proceeding by it in respect thereof is in the public interest, hereby issues its complaint, charging as follows:

E. I. DUPONT DE NEMOURS & COMPANY

1. Respondent E.I. DuPont de Nemours & Company (hereinafter "DuPont") is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its principal offices and place of business located at 1007 Market St., Wilmington, Delaware.

2. DuPont is engaged principally in manufacturing and selling diversified lines of chemical products and other products related thereto. In 1976, the company's sales were in excess of $8.3 billion, its net income was in excess of $459 million, its assets at year end were valued in excess of $7 billion, and it ranked 16th on the Fortune 500 list.

[1] Mark I. Levy, Esq., was on the briefs for respondent. He is now Assistant to the Solicitor General, Office of the Solicitor General of the United States, Department of Justice, Washington, D. C. 20530.

3. DuPont is the dominant domestic producer of titanium dioxide pigments (hereinafter "TiO_2"), presently accounting for more than 40% of domestic annual production. In 1976, TiO_2 produced by the company in the United States was valued in excess of $265 million, yielding the company pre-tax earnings of approximately $40 million. [2]

4. At all times relevant hereto, DuPont sold and shipped its products throughout the United States, and engaged in or affected commerce within the meaning of Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. 44.

TRADE AND COMMERCE

5. For purposes of this complaint, the relevant market is the production of TiO_2 in the United States.

6. TiO_2 produced in the United States in 1976 was valued in excess of $600 million.

7. The relevant market is highly concentrated, with the top four firms accounting for more than 80% of production.

8. Barriers to entry into the relevant market are high.

9. Except to the extent that competition has been hindered, frustrated, lessened, or eliminated by the acts and practices alleged in this complaint, DuPont is in substantial competition with other firms in the relevant market.

ACTS AND PRACTICES

10. Since as early as 1972, DuPont has engaged and is now engaging in unfair methods of competition and unfair acts and practices in or affecting commerce by using its dominant position, size and economic power in an attempt to monopolize the relevant market alleged herein. Said unfair methods of competition and unfair acts and practices by DuPont have included, but have not been limited to, the following:

a. adoption and implementation of a plan to expand the company's domestic TiO_2 production capacity by an amount sufficient to enable the company to capture substantially all growth in domestic demand for TiO_2 through at least the 1980's; and

b. adoption and implementation of a pricing policy designed to frustrate the growth of smaller domestic TiO_2 producers and to forestall entry by foreign producers. [3]

EFFECTS AND VIOLATION

11. The aforesaid acts and practices have had and do have, among other things, the tendency and capacity to restrain, lessen, or eliminate competition or to create a monopoly in the relevant market alleged herein, and thus are to the prejudice and injury of the public and constitute unfair methods of competition and unfair acts and practices in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act, as amended.

Initial Decision by Miles J. Brown, Administrative Law Judge

August 31, 1979

Introduction

The Federal Trade Commission issued its complaint in this matter on April 5, 1978 (mailed April 10, 1978), charging respondent, E. I. DuPont de Nemours & Company ("DuPont") with unfair methods of competition and unfair acts and practices in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act, as amended (15 U.S.C. 45).

More particularly, the Commission charged that DuPont had, since as early as 1972, engaged in certain practices in an [2]attempt to monopolize the production of titanium dioxide pigments ("TiO_2") in the United States. The Commission alleged that the practices challenged included, but were not limited to, the following:

a. adoption and implementation of a plan to expand the company's domestic TiO_2 production capacity by an amount sufficient to enable the company to capture substantially all growth in domestic demand for TiO_2 through at least the 1980's; and

b. adoption and implementation of a pricing policy designed to frustrate the growth of smaller domestic TiO_2 producers and to forestall entry by foreign producers.

The complaint alleged that DuPont's practices had the tendency and capacity to restrain, lessen or eliminate competition or to create a monopoly in the relevant TiO_2 market and were to the prejudice and injury of the public and constituted unfair methods of competition in violation of Section 5 (see Complaint).

In the notice of contemplated relief that accompanied the complaint, the Commission suggested, among other things, (1) the divestiture of DuPont's De Lisle, Mississippi, TiO_2 production facility

as a viable, independent entity; (2) divestiture of either DuPont's New Johnsonville, Tennessee, TiO_2 facility or of DuPont's Edge Moor, Delaware, TiO_2 facility as a viable, independent entity; and (3) royalty-free licensing of all "technology and know-how" used by DuPont in connection with the production of TiO_2 (Complaint p. 5).

In its answer, DuPont asserted that the complaint failed to set forth a violation of Section 5 of the Federal Trade Commission Act or any other provision of law. As to the challenged practices spelled out in the complaint, DuPont asserted that it has lawfully expanded its capacity to produce TiO_2 in anticipation of increased demand and has at all times lawfully priced its products. Among its specific defenses, DuPont contended that the Commission lacks statutory authority to order the relief set forth in the notice of contemplated relief and that any sanction, such as divestiture or royalty-free licensing, would infringe upon DuPont's right to due process of law as guaranteed by the Fifth Amendment to the Constitution of the United States (see Answer).

Thereafter complaint counsel engaged in intensive discovery of DuPont, DuPont's TiO_2 competitors and certain TiO_2 users. The return on complaint counsel's discovery of nonparties was made available to DuPont. Confidential information was subject to strict protective orders limiting access thereto to DuPont's independent "outside" counsel. During this same period, DuPont engaged in discovery directed to the Commission and, later to its TiO_2 competitors. Following the exchange of trial briefs, witness and exhibit lists, adjudicative hearings [3]commenced on December 20, 1978, at which time complaint counsel presented the bulk of their documentary exhibits. DuPont's requests for *in camera* treatment for certain exhibits were granted (see tr 5–20).[2]

On January 8, 1979, a hearing was held on the question of the confidential status of certain production statistics of nonparty competitors which were the basis for complaint counsel's statistical charts, the final forms of which are in the record as CXs 220–227.[3] Although NL Industries ("NL"), formerly National Lead Co., Gulf and Western ("G&W") and American Cyanamid ("Cyanamid") registered strong objections to certain procedures employed by the administrative law judge resulting in the publication of the preliminary drafts of the charts themselves, the problems relating to the

[2] All *in camera* treatment for DuPont's confidential documents was granted with the understanding that *in camera* status would expire on the date of the initial decision. On August 10, 1979, the administrative law judge issued an order extending *in camera* treatment for these documents until issuance of the final order by the Commission or unless otherwise ordered by the Commission.

[3] DuPont and complaint counsel stipulated that the charts would be considered accurate for purposes of this proceeding only, thus settling all controversies as to whether different methods of calculating values were used by the various reporting sources and all other questions regarding compilation of industry data (CXs 228A–E; 229).

underlying documents were resolved by deleting certain sensitive information not necessary to the adjudication of any of the issues in this matter.

Complaint counsel presented one witness, Dr. William G. Shepherd, Professor of Economics, University of Michigan. His direct testimony was reduced to writing in advance of hearings (CX 218). The cross examination, redirect examination and recross examination of Dr. Shepherd consumed three hearing days (tr 129–582).

On February 12, 1979, complaint counsel's "charts" (CX 220–227) were received into evidence, whereupon complaint counsel rested their case-in-chief (tr 596).[4] DuPont immediately began its answering case and in six days of hearings introduced the testimony of four top DuPont officials[5] and the testimony of Elaine Donald, Manager of Marketing Analysis in the Chemical, Dye and Pigment Department (tr 955–1007; 1172–1192).

On February 26, 1979, DuPont presented the direct [4]testimony of Dr. Morris Albert Adelman, Professor of Economics, Massachusetts Institute of Technology (tr 1530–1617). The cross examination, redirect examination and recross examination of Dr. Adelman was heard on March 1, 1979, after which DuPont offered several documentary exhibits into evidence and rested its answering case (tr 1628–1782). On March 16, 1979, the fourteenth and last day of hearings, complaint counsel offered their case in rebuttal, consisting solely of documentary exhibits (tr 1792–1851). DuPont's surrebuttal consisted of two documents that were received into the record by order dated March 26, 1979.

On April 16, 1979, after having been advised that the Official Reporter had delivered the record to the Office of the Secretary, the administrative law judge closed the record for further receipt of evidence, and set a schedule for the filing of proposed findings and briefs. The parties filed their proposed findings on May 16, 1979, and their answering briefs on June 5, 1979. On July 9, 1979, the Commission granted the administrative law judge's request for an extension of time until August 24, 1979, in which to file the initial decision, and on August 21, 1979, further extended this time until August 31, 1979.

Any motions appearing on the record not heretofore specifically ruled upon either directly or by the necessary effect on the

[4] Respondent's motion to dismiss at the close of the case-in-chief was denied (tr 584–5; 596).

[5] Crawford H. Greenewalt, past President and past Chairman of Board of Directors (tr 597–658); Irving S. Shapiro, current Chairman of the Board of Directors and Chairman of the Executive Committee (tr 659–868); James H. Baird, General Manager of the Chemicals, Dyes and Pigments Department (created January 1978) and past Assistant General Manager of the Pigments Department (tr 869–954, 1013–1171; 1198–1227); and Harold B. Clark, Manager, Research and Development for White Pigments and Mineral Products (tr 1229–1518).

conclusions in this initial decision are hereby denied. The proposed findings and conclusions submitted by counsel supporting the complaint ("CSCPF") and counsel for DuPont ("RespPF")[6] have been given careful consideration and to the extent not adopted by this decision, in the form proposed or in substance, are rejected as not supported by the evidence, as argumentative, or as immaterial.

Preliminary Statement

The record in this case consists primarily of documents created in the normal course of DuPont's TiO_2 business. These documents include requests for appropriations for plant construction or expansion, annual reports of the Pigment Department to the Executive Committee, and Pigments Department "Task Force" analyses of the TiO_2 industry and DuPont's TiO_2 business. The record also includes the testimony of some of DuPont's top officials entrusted with making or recommending decisions relating to the TiO_2 business. DuPont's answer to complaint counsel's request for admissions (CX 3) contains many of the evidentiary facts of this case. [5]

There is little dispute as to the actual events that took place during the critical period from 1971 to 1978. The parties are, however, in total disagreement as to the meaning, weight, and importance that are to be accorded certain documents and statements contained therein.[7] Although a long, and perhaps too detailed, recitation of the facts annotated to the record is included in this initial decision, it is appropriate, I think, at the outset, to summarize the findings and the factual issues raised by the parties.

Summary of the Findings

TiO_2 is a white chemical pigment employed in the manufacture of other products to make them whiter or opaque and it is used primarily by the manufacturers of paints, paper, synthetic fibers, plastics, ink and synthetic rubber.

There are two basic processes used in the manufacture of TiO_2. The "sulfate" process which uses a sulfuric acid reaction on a relatively low grade feedstock (ilmenite ore or titanium slag) and a "chloride" process which uses a chlorine reaction upon either a high grade titanium ore feedstock (rutile ore or synthetic rutile) or on

[6] Other abbreviations used in this initial decision are: CX—Commission's Exhibit; RX—DuPont's exhibit; RespBr—Brief in Support of Proposed Findings of Facts and Conclusions for DuPont; CSCReply—complaint counsel's reply to DuPont's proposed findings; RespReply—Reply Brief of DuPont; and tr—transcript of testimony.

[7] Many of these "events" were intracorporate communications, pertinent portions of which have been set forth verbatim in the "Findings as to the Facts" section which begins at page 8, *infra*.

lower grades of feedstock (primarily ilmenite ore). Only DuPont used the chloride process with lower grade feedstocks.

The so-called sulfate process was developed first. Because it is a "batch" process, as contrasted with the "continuous flow" operation of the chloride process, the sulfate process is not as conducive to scale economies. Following World War II, DuPont, already operating several sulfate TiO_2 plants, decided to try to develop a commercially feasible ilmenite chloride process using the relatively abundant low grade ilmenite ore. By 1953 DuPont had built a fully operational production unit at its Edge Moor, Delaware, facility. By 1958 it had built another plant at New Johnsonville, Tennessee, utilizing its "ilmenite chloride technology." During this period, other TiO_2 manufacturers built sulfate process plants.

In the late 1950's abundant rutile ore deposits were discovered. From 1960 until 1970 all TiO_2 plants constructed (including DuPont's Antioch, California, plant) were designed to use this high grade rutile ore in a rutile chloride process. Until the late 1960's, the overall costs of production were substantially identical in the various processes and except for short periods of time, the TiO_2 market was stable and enjoyed a steady growth. DuPont did enjoy some economies of scale at its large New Johnsonville facility and to a lesser degree at its, by then enlarged, Edge Moor chloride plant. Although only DuPont had the technological "know-how" for a commercially [6]feasible chloride process on the lower grade ilmenite ore feedstock, the relative costs of rutile feedstock and ilmenite were such that none of the manufacturing processes enjoyed a significant cost advantage.

The cost of rutile ore increased dramatically in the late 1960's and early 1970's. At about the same time, environmental regulations required the TiO_2 manufacturers using the sulphate process to embark on costly pollution abatement programs. As a result, DuPont's ilmenite chloride process for TiO_2 placed it at a substantial cost advantage when compared with its competitors bound by either the sulphate process or the high quality rutile feedstock chloride process.

In 1972, DuPont decided to capitalize on this cost advantage by engaging in a growth strategy. It continued the policy of refusing to license its ilmenite chloride technology, accelerated and increased the expansion of its Edge Moor and New Johnsonville plants and initiated plans to construct a large new plant using the advanced chloride technology. DuPont anticipated being able to supply the market place with all of the additional needs for TiO_2 (resulting from growth in market demand of TiO_2 or through withdrawal of its

competitors from TiO_2 production) through the 1980's. The company estimated that it would obtain about 65% of the TiO_2 market by 1985. In 1975, a time of recession, DuPont reviewed its 1972 strategy and decided to continue with its program of "aggressive expansion," including the construction of a new plant at De Lisle, Mississippi.

From 1972 to 1976, DuPont's share of the domestic TiO_2 market rose from approximately 30% to approximately 41% and by 1977 it had achieved a 42% share of that market. However, due to the slowdown in the economy, the total consumption of TiO_2 in 1977 was not significantly different than it was in 1972.[8] Although the demand for TiO_2 has not increased as expected through 1978, DuPont still forecasts that it will obtain about a 55% share of the market by 1985 and admits that its 1972 growth strategy is still in effect.

Since 1970, no competitor has embarked on a program of expansion and since 1974 DuPont has impeded certain price rise attempts by its competitors.

Complaint counsel's theory of the case is that, in 1972, when DuPont was placed at a substantial cost advantage over its TiO_2 manufacturing competitors through the "fortuitous" increase in the price of rutile ore and the increase in the cost of waste disposal from the sulfate process of manufacturing TiO_2, it devised an "aggressive growth strategy" by which it [7]planned to capture substantially all of the growth in the TiO_2 market until the mid-1980's. Complaint counsel contend that in implementing this growth strategy, DuPont embarked on an unwarranted capacity expansion program combined with a strategic pricing program whereby it would price high enough to finance its expansion but yet not high enough to warrant competitors to expand.

According to complaint counsel, DuPont's growth strategy unreasonably prevented its competitors from expanding and thus prevented them from building large TiO_2 plants with which to learn the low grade ore ilmenite technology or to take advantage of economies of scale. Complaint counsel assert that by such practices and by the refusal to license its low grade ore ilmenite technology to NL or any other domestic manufacturer, DuPont has unreasonably protected its cost advantage from competitive erosion and, accordingly, it is in a position to gain a monopolistic share of the TiO_2 market in the future.

Complaint counsel admit that each facet of DuPont's strategy is not objectionable taken by itself. Their theory of violation of Section

[8] Several TiO_2 competitors closed their rutile chloride process plants in the early 1970's, and NL closed its St. Louis sulfate plant in 1978 because of environmental difficulties. Kerr-McGee built a large beneficiation plant to produce synthetic rutile but recently discontinued production due to inefficiencies in the operation.

5 of the Federal Trade Commission Act is the exclusionary effect of DuPont's aggressive growth strategy taken as a whole, and the anticompetitive effects that may result therefrom (see CSCPF pp. 2–3, 85–86, 123–25; CSCReply pp. 5–6).

DuPont admits that its long term strategy was to take advantage of the unique opportunity it had through its cost superiority over its competitors to capture substantially all of the growth in the TiO_2 market until the mid-1980's (RespReply 1, 7). However, it denies that its cost advantage was entirely "fortuitous," but instead was the outcome of its business decision to innovate the low grade ore technology many years before (RespBr pp. 5–6; RespReply A8–9). It denies that its expansion of capacity of existing plants or the building of the De Lisle plant was anything more than preparing to satisfy the increase in demand expected in the TiO_2 market (RespPF # 59; RespReply A21–A23). It also denies that it engaged in any pricing practice that could be considered to be unlawful, and asserts that it did not adopt or implement the strategic pricing asserted by complaint counsel (RespPF #145; RespReply A16–A19).

DuPont claims that there was nothing to prevent its competitors, who are large corporations experienced in the rutile chloride process for manufacturing TiO_2, from perfecting their own low grade ore technology or building large scale manufacturing plants, if they chose to engage in those areas of investment (see RespPF ##252–273; RespReply A25–A28). DuPont states that it was under no obligation to license its low grade ore technology to NL or any other competitor (RespPF #108; RespReply A24–25). Finally, DuPont points out that the record shows that it has not achieved the increase in market share anticipated in its growth strategy, and that in the competitive atmosphere that presently exists in the TiO_2 [8]market, it is in no position to acquire a monopoly in that market (RespPF ## 209–248; RespReply 8, A6–A7, A33–A36).

DuPont claims that complaint counsel have placed unwarranted emphasis on certain statements contained in "task force" related documents that actually reflected "think tank" or "brainstorming" type exercises, and which, according to DuPont officials, were not relied upon by management in making its business decisions and were not the basis for such decisions (see RespPF ## 180–186; RespReply A18–19). DuPont points to the testimony of its officials to support its view that such decisions did not involve strategic pricing or other exclusionary tactics (RespReply A19).

Having reviewed the entire record in this proceeding, and having considered the demeanor of the witnesses together with the pleadings, the proposed findings, conclusions and briefs submitted by

complaint counsel and counsel for DuPont, I make the following findings of fact based on the record considered as a whole:

Findings of Fact

1. DuPont is a Delaware corporation with its principal place of business located at 1007 Market St., Wilmington, Delaware. At all times relevant hereto, DuPont sold and shipped its products throughout the United States and engaged in or affected commerce within the meaning of Section 4 of the Federal Trade Commission Act, as amended (see Complaint and Answer ¶¶ 1, 4).

2. DuPont is engaged in the manufacture and sale of a diversified line of chemical and related products which may be generally classified as follows: agricultural chemicals; industrial chemicals; explosives; finishes and coated fabrics; textile fibers; pharmaceuticals; photographic products; synthetic rubber products; polymer intermediates; plastics, resins, coatings and films; and pigments and dyes (see CX 65J, K). DuPont sells primarily to other manufacturers, with a relatively small portion of its products reaching the consumers in the form produced by it (CXs 4–8, 9Z17–18, 65J, K).

3. Until January 1, 1978, DuPont's TiO_2 business was part of the Pigments Department, which on that date was merged with the Dyes and Chemical Division to form the Chemicals, Dyes and Pigments Department (see CX 9Z16; tr 869 (Baird)).

4. The relevant product market for purposes of this case is [9] TiO_2 pigments ("TiO_2") (CSCPF #5; RespPF #209).[9]

5. The United States as a whole is the relevant geographic market for purposes of this case (CSCPF #5; RespPF #209).

6. In 1976, DuPont had total sales in excess of $8.3 billion, assets in excess of $7 billion and net income in excess of $459 million. In 1976, DuPont's production of TiO_2 was valued at approximately $265 million, and sales of such products yielded the company pretax earnings of approximately $40 million (Complaint and Answer ¶¶ 2, 3; CX 8). In 1976, the value of DuPont's total domestic shipment of TiO_2 was $257 million (CX 222).

7. In 1976, DuPont had five manufacturing competitors in the domestic TiO_2 market, all of which manufactured a diversified line of products (see CXs 220–227; RX 46, 47, 49, 50, 86). They were G&W, Cyanamid, Kerr-McGee, NL and SCM.

8. TiO_2 is a white pigment used to whiten, brighten and opacify

[9] The parties have agreed that market shares for purposes of this case are to be calculated from domestic shipments of TiO_2 (CX 223; see tr 1118–19).

paints, plastics, paper, inks, synthetic fibers and rubber compounds (CX 3 ## 1, 2, 4; CXs 9H; 75B; 120Q; 140B).[10] Due to its unparalleled quality as a white pigment, TiO_2 has no commercially satisfactory substitute over a wide range of prices, and no significant future substitutes providing comparable "value-in-use" are foreseen (CX 3 ## 61–63; CX 9H).

9. There are three titaniferous feedstocks used in the manufacture of TiO_2: (1) titaniferous mineral concentrates—ilmenite, rutile and leucoxene—each of which is derived from a naturally occurring ore of the same name; (2) titanium slag, which is produced by smelting ilmenite concentrate; and (3) beneficiated titaniferous concentrates, commonly referred to as "synthetic rutile" or "beneficiated ilmenite", which are ilmenite concentrates processed and upgraded to be roughly equivalent to rutile concentrates (CX 3 ##29, 30; CX 191A; tr 614 (Greenewalt)).

10. Titanium ores are always found associated with iron with the ratio of iron to titanium dioxide being highest in rock type ores and lowest in rutile ore (tr 614–15 (Greenewalt)). The various titaniferous feedstocks differ in titanium dioxide content, a factor that affects the suitability of the feedstock [10]for a particular process, as well as the amount of waste product produced. The titaniferous feedstocks used in the manufacture of TiO_2 have the following titanium dioxide content: ilmenite concentrate—30% to 80%; titanium slag—70% to 85%; leucoxene—less than 90%; synthetic rutile—90%—95%; and rutile concentrate—90% to 99% (CX 3 ## 31–34; CX 131C).

11. The domestic TiO_2 producers using natural rutile ore currently rely almost entirely on foreign sources, with the only known large deposits of economically extractable rutile ore being located in eastern Australia (CX 3 #45; tr 643 (Greenewalt); see CX 266Z4). The more abundant ilmenite ore is mined in Florida, New Jersey and New York as well as in western Australia (CX 266Z2, Z4). Substantial quantities of titanium slag are imported from Canada (CX 266Z4).

12. For purposes of this case there are *three*[11] commercial processes used to produce TiO_2: (1) the sulfate process; (2) a high-grade feedstock chloride process which may be called a "rutile chloride process"; and (3) a low grade feedstock chloride process,

[10] TiO_2 exists in two different crystal structures, rutile (in no way related to "rutile" ore) and anatase. Anatase TiO_2 is used primarily in the paper industry. Because rutile TiO_2 requires an additional step in the sulfate process, anatase TiO_2 is somewhat cheaper than rutile TiO_2. DuPont is the only manufacturer able to produce anatase TiO_2 by the chloride process (CX 3, ## 50, 56–59; CXs 17D, H; tr 892–93 (Baird)).

[11] From a technical or scientific view there are only *two* processes, the sulfate process and the chloride process. The chloride process, in turn, has two categories relating to the feedstocks used. DuPont's ilmenite or advanced chloride process is not separable so much because of the basic chemistry involved, but because of the advanced technology necessary to create a feasible commercial manufacturing operation using that process.

used only by DuPont, which may be called the "ilmenite chloride process" or the "advanced chloride process" (CX 3 ## 14, 39, 40). In the sulfate process, by which TiO_2 is produced by the digestion of titaniferous feedstocks with sulfuric acid, only ilmenite and titanium slag can be used. In the chloride processes, titanium bearing ores are reacted with chlorine in the presence of carbon to yield titanium tetrachloride which in turn, when combined with oxygen, forms titanium dioxide (CX3 ## 12, 13; CXs 9H, 14Z29-Z31, 58H, 61A; 266M). The rutile chloride process requires the use of rutile or synthetic rutile. The ilmenite (or advanced) chloride process uses feedstocks consisting of a mixture of ilmenite, leucoxene and rutile ranging from 60% to 70% natural titanium dioxide content (CX 3 ## 14, 39, 40; CXs 14, 58E, 72A, 117 *in camera*).

13. The first domestic plant for manufacturing TiO_2 was built by National Lead Co. at Sayreville, New Jersey. It began operations in 1918. This was a sulfate process plant. National Lead built a second sulfate process plant in 1923, at St. Louis, Missouri (see CX 3 #144).

DuPont entered the TiO_2 business in 1931 when it acquired the Commercial Pigment Company which operated a sulfate process TiO_2 plant in Baltimore, Maryland. In 1935, DuPont built a sulfate process TiO_2 plant at Edge Moor, Delaware (CX 3 ## 91, 92, 95; CXs 15A, 241A *in camera*).

Virginia Chemical Company, which by 1947 had become a [11] subsidiary of Cyanamid, began producing TiO_2 by the sulfate process in 1937 at a plant at Piney River, Virginia (CX 3 ## 152, 153).[12]

Glidden Paint Company (eventually acquired by SCM in 1967) started a sulfate process TiO_2 plant at Baltimore, Maryland, in 1956 (see CX 266Z9; CX 3 #167).

In 1948, DuPont completed construction of a chloride process plant at its Edge Moor facility. By 1952 this plant was successfully producing TiO_2 using a low grade ore feedstock (see Finding 16, *infra*).

In 1955, Cyanamid began producing TiO_2 at Savannah, Georgia, using the sulfate process (CX 266Z7).

New Jersey Zinc Company began producing TiO_2 by the sulfate process at Gloucester, New Jersey, in 1956. It became a subsidiary of G&W in 1966 (CX 3 ## 161-162).

In 1958, DuPont started up a new ilmenite chloride process plant at New Johnsonville, Tennessee.

14. In the late 1950's or early 1960's large quantities of rutile ore were discovered in Eastern Australia. All new TiO_2 production

[12] See CX 266Z7-Z10 for a list of TiO_2 producing companies, their plant locations, the process and raw materials used, and an estimated name plate capacity history with planned expansions.

plants constructed after that discovery were designed to use a rutile chloride process (see CX 16A). In 1964, DuPont opened a plant using a rutile chloride process at Antioch, California (CX 266Z7).

In 1964 Cabot Corporation opened a rutile chloride process TiO_2 plant in Astabula, Ohio. In 1965 American Potash Chemical Corporation (subsequently acquired by Kerr-McGee) opened a rutile chloride plant at Hamilton, Mississippi (CX 3 #159; CX 266Z7). In 1966, Cyanamid opened a rutile chloride process TiO_2 plant at Savannah, Georgia and NL opened a rutile chloride process plant at Sayreville, New Jersey. In 1968, SCM opened a rutile chloride process plant at Baltimore, Maryland, and PPG (Pittsburg Plate Glass) opened a rutile chloride process plant at Natrium, West Virginia (CX 3 ## 155–171).

In 1970, Sherwin Williams opened a rutile chloride process plant in Astabula, Ohio. This plant was built for Sherwin Williams by DuPont (see CX 33C). SCM purchased this plant in 1974, with the approval of DuPont.

15. Some of the considerations that led DuPont to undertake development of a chloride process were the desire to achieve greater ore flexibility and to reduce waste disposal problems. The sulfate process can use only those ores that react with [12]sulfuric acid. At that time, there were abundant titanium ores unsuitable for use in the sulfate process. In addition, DuPont wished to use the lower grade ilmenite because it had a readily available supply, originally from India, and later from Florida (CX 16I, J; tr 1417–19 (Clark)).

In the sulfate process approximately three and one-half tons of waste are produced for every ton of TiO_2. It is difficult to dispose of this waste, a solution of iron sulfate and sulfuric acid.

In contrast, the rutile chloride process yields only one-half ton of waste per ton of TiO_2. In addition, the principal chloride process waste comes out as dry anhydrous ferric chloride which is easier to dispose of than the acidic waste from the sulfate process. The low grade ilmenite chloride process yields more waste per ton of TiO_2 produced than the rutile chloride process (tr 1071–72 (Baird)).

16. The development of DuPont's ilmenite chloride process, including its progression from laboratory to production plant, proved to be a very difficult technical feat. Although DuPont had demonstrated the practicality of operating small chloride process experimental units, this small scale production experience could not be extrapolated to larger commercial production units. Instead, it was necessary to discard or radically modify many of the small scale

336-345 O - 81 - 43

techniques and devise new ones applicable at large scale (CX 241D, *in camera*).[13] Increases in the size of equipment and the scale of the operation materially changed the operating characteristics (ibid).

The original 12,000 ton per year TiO_2 chloride plant at Edge Moor was completed and ready for initial operating trials in the Spring of 1948. It was not until 1951 that the problems with the chloride process were overcome. By 1952 DuPont had a commercially viable chloride TiO_2 production process using low grade ilmenite feedstocks (CX 24IE, *in camera*; tr 618, 637, 650 (Greenewalt)). In 1956, the chloride process facility at Edge Moor was expanded with a second chloride unit (RX 3Z1–Z2) and by 1965 the capacity of that chloride facility was 45,000 tons per year. In 1958–59 DuPont built a new chloride facility at New Johnsonville, Tennessee (RX 3Z1-Z2). This new facility was at large scale to take advantage of scale economies and in 1959 DuPont produced 45,000 tons of TiO_2 there (CX 241N, *in camera*; RX 3Z1). Significantly, although it only took six months to move the New Johnsonville plant from initial trials to a viable production facility, it was not until 1963 that the New [13]Johnsonville plant was operating at maximum efficiency (see CX 212J). New Johnsonville's production capacity was expanded to 70,000 tons per year by 1963, to 100,000 tons per year by 1964, and to 120,000 tons per year by 1968. DuPont enjoyed substantial scale economies at the New Johnsonville plant by 1970 (CX 3 ## 20, 21; RX 3Z1).

17. Subsequent to the development of DuPont's ilmenite chloride process, large deposits of rutile ore became available (tr 642–43 (Greenewalt); tr 1420–21 (Clark)). This readily available source of high grade ore encouraged TiO_2 producers, including DuPont (Antioch, California), to build rutile chloride plants during the 1960's (see *Finding* 14, *supra*). A high grade rutile process plant was considered to yield at that time a better return on investment than a comparable low grade ilmenite process plant, considering the relative cost of the raw materials (rutile and ilmenite), the cost of chlorine, the cost of disposing of waste materials, and the lower cost of the initial investment for a high grade ore plant (tr 1071–72 (Baird); tr 1473–74 (Clark); RX 20E; CX 16A, C).[14]

18. DuPont's New Johnsonville ilmenite chloride process plant produced a higher quality pigment than the sulfate plants. On the

[13] Exhibit CX 241, *in camera*, spells out the development of the chloride process and details many of the technical difficulties encountered. For example, one difficult problem encountered was the development of materials that would hold up in the extremely corrosive environment of chlorine gas at very high temperatures. Mr. Greenewalt summarized the development of the low grade TiO_2 technology (tr 608–26).

[14] The ilmenite chloride process consumes more chlorine per ton of TiO_2 produced and turns out more waste, than the high grade rutile chloride process.

basis of its experience at New Johnsonville, DuPont's officials made the following assessment in May of 1972 (CX 26B):

> . . . The success of the Johnsonville process resulted in a rapid increase in share of market as the quality and adequate supply of the improved pigment became the standard of comparison in the industry . . .

19. The 1960's had been a stable and relatively profitable period for TiO_2 producers, although imports caused problems at times (CX 250B; tr 670–71 (Shapiro)). In the 1950's and 1960's the selling price of TiO_2 had remained essentially unchanged. As imports and domestic capacity increased in the 1960's, price cutting became prevalent. And by the end of 1969 the economy began to enter a recession (CX 250B; tr 671, 677 (Shapiro); tr 872–73 (Baird); tr 1232–33 (Clark)).

DuPont's profitability in TiO_2 was extremely attractive in the 1960's. Between 1965 and 1970, the net rate of return (after taxes) was between 10.3 and 15.5%, averaging 12.5%, and was probably greater in the first part of the 1960's (CXs 115G; 26B; tr 671 (Shapiro)).

20. By 1970, there were nine producers of TiO_2 in the United States. As reported on CX 221 (Appendix A), the total ("name plate") capacity for 1970 was as follows (thousands of tons): [14]

	Capacity	%
NL	268	32
DuPont	252	30
Cyanamid	90	10.7
SCM	78	9.3
G&W	43)	8.3[15]
Cabot	27)	
Kerr-McGee	37	4.4
Sherwin Williams	27	3.2
PPG	18	2.1

As reported on CX 224 and CX 225 (Appendix D and E) the domestic production of TiO_2 by the sulfate and chloride processes was as follows in 1970 (thousands of tons):

[15] G&W and Cabot's capacities have been counted together on CX 221.

	Sulfate	Chloride
NL	192.9	28.8
DuPont	42.8	161.0[16]
Cyanamid	47.4	6.4
SCM	48.4	.7
G&W	33.0	–
Kerr-McGee	–	33.4
Sherwin Williams	–	18.4
Cabot	–	21.4
PPG	–	10.3

21. Shortly after 1970, an unexpected shortage of rutile ore developed and the price of rutile ore increased dramatically (RX 20; tr 1421 (Clark)). In early 1972, with the cost of high grade rutile feed stocks at all time levels, some competitive TiO_2 producers curtailed their operations. PPG abandoned its rutile chloride process plant at Natrium, West Virginia, and NL shut down its rutile chloride process unit at Sayreville, New Jersey. In 1972, G&W leased Cabot's rutile chloride process plant located at Astabula, Ohio, with an option to buy, which it exercised in 1975 (CX 3 #166). In 1974, SCM purchased the Sherwin Williams rutile chloride process plant at Astabula, Ohio (CX 3 #142).

22. In early 1970, following enactment of environmental legislation, sulfate producers, reputed to be worst of the chemical industry polluters, were forced to incur substantial pollution related capital investment costs, greatly raising the costs of these plants (CXs 27, 34H).

23. By early 1972, the increase in the price of rutile ore vis-a-vis ilmenite ore and the increased costs for pollution abatement for the sulfate process producers vis-a-vis the chloride process producers, placed DuPont at a significant cost advantage over all of its competitors, an advantage that was [15]further magnified by economies of scale enjoyed by DuPont's New Johnsonville and Edge Moor ilmenite chloride process plants. In addition, because of the shut down of some rutile chloride process plants and reduced imports, a severe shortage of TiO_2 was experienced in the domestic TiO_2 market (CX 3 ## 172–178).

24. In February 1972, DuPont announced plans to complete the conversion of Edge Moor to an all ilmenite chloride facility, thus

[16] DuPont's production of TiO_2 uses the ilmenite chloride process except for 27,000 tons produced at its Antioch, California, plant, which uses a rutile chloride process (see CX 266Z7–Z8).

eliminating the last of its sulfate process production (see CX 17B-F). Replacement of its sulfate facility was made feasible through the development of techniques to produce an anatase-type TiO_2 by the chloride process (see CXs 17, 21).[17] It also planned the expansion of the New Johnsonville plant. The capacity available from existing plants after expansion was expected to be sufficient to supply demand to 1979–1981, before additional manufacturing facilities would be needed (CX 21K). DuPont also planned to close its Antioch, California, rutile chloride plant as soon as practicable, thus eliminating any dependence on rutile ore (Ibid.).

25. In 1971, the Pigments Department had created a TiO_2 "Task Force" and "Core Group". The Core Group consisted of the heads of the divisions in the Pigments Department who were responsible for the various aspects of the TiO_2 business. The Task Force was made up of a number of individuals in the Pigments Department at the level below the division heads. The Task Force also created certain sub-groups called "Task Groups" to study various issues. The Task Force reported to the Core Group, which in turn reported to the Pigments Department through Mr. Baird, the Assistant General Manager. In 1972, the Task Force engaged in a broad evaluation of DuPont's TiO_2 business and made recommendations for a long-range strategy, the final details of which were reported to the Executive Committee in May, 1972 (tr 871–75 (Baird); 1231–32 (Clark); see CX 73A).

26. In a document dated May 25, 1972 ("1972 White Paper") A. H. Geil, Vice-president & General Manager, Pigment Department, reported to the Executive Committee on "Opportunities in the TiO_2 Business." The 1972 White Paper, in pertinent part reads (CX 26, 27):

. . . A number of significant developments have occurred which make it desirable at this time to reassess the outlook for this business and to request your Committee's concurrence with the broad outlines of a program designed to take advantage of significantly enlarged opportunities [CX 26A].

* * * * * * *

. . . The price competition of the 1965 to 1971 [16]period narrowed profit margins for all producers in the industry, and brought home as never before the realities of the business. The most significant of these include:

At substantial scale, the chloride process requires lower capital investment than the sulfate process.

Disposal of wastes from the chloride process can be accomplished at a lower economic penalty than is the case with the sulfate process.

[17] Anatase TiO_2 is used by paper manufacturers, and constitutes approximately 20% of DuPont's domestic shipments of TiO_2 (see CX 68J).

With the exception of DuPont, all other producers by the chloride process require the use of either rutile ore or a beneficiated product having a low iron content. The world-wide shortage of rutile has resulted in an increase in price from $A65 in 1965 to $A110 in 1972 [CX 26B].

With completion of the conversion of the Edge Moor sulfate unit to a chloride process operation, DuPont will be entirely committed to chloride process operations at large scale. DuPont's unique ability to operate the chloride process with relatively low cost ilmenite ore provides a favorable operating cost capability. Technology for complete recycle of process wastes with an acceptable economic penalty is progressing. *This combination of factors puts DuPont in a unique position to increase its share of market by a substantial amount.*

Competitive developments during the past six months provide support for this contention. PPG Industries recently announced the abandonment of its chloride process plant because of unfavorable prospective economics. This move coincided with the failure of the Sherbro project in Sierra Leone which was designed to provide the rutile feed for this unit. NL Industries has announced abandonment of its chloride process unit as a result of unfavorable economics. This producer has also terminated its production of an extended titanium pigment under conditions which have alienated some of the customers formerly purchasing that product. Concurrent with these events has been the effect of the government's monetary actions on importation of titanium dioxide. The import surcharge and, subsequently, the devaluation of the dollar have made imported [17]products less competitive in this market.

Assessment of the status of competitive producers leads to the conclusion that sulfate process operators, with the exception of NL Industries, will be unable to cope with waste disposal problems and will shut down eventually. Chloride process producers probably will continue operations, but it is difficult to see how they can cope with waste disposal and generate sufficient funds for major expansion. [CX 26C].

The combination of these factors has narrowed the margin between total production capacity in this country and the level of consumer demand. Pigments Department has been oversold since early in the year, and information from the trade indicates that American Cyanamid and other producers in varying degree are in this position.

For the short term, Pigments Department is taking steps to increase production capacity as expeditiously as possible. The plant shutdown of the Antioch unit has been deferred. The expansion at Johnsonville is being expedited in order to achieve partial expansion at the earliest date. Modest capacity increases at Edge Moor are being undertaken. In view of the prospects, however, these are stop-gap measures.

Continued growth of the TiO_2 market is forecast. While the rate of population increase has declined, TiO_2 has demonstrated a consistent increase in per capita consumption. In terms of total impact, TiO_2 can be described as a "standard of living" product. Its per capita consumption has paralleled the per capita consumption of electrical energy, for instance. Technologically, the only threats to TiO_2 as the major pigment of commerce are silicon carbide and "void hiding" products. It is concluded that silicon carbide would be too expensive to compete. Void hiding can be achieved by encapsulating tiny air bubbles and TiO_2 particles for certain emulsion paint and paper applications. Realistic potential for these products is included in sales projections.

It is expected that the domestic industry requirements will grow at a rate of about 3.5% per year for the balance of this decade. In terms of industry tonnage, this means that requirements will be between 1,000M[18] and 1,100M tons in 1980, as compared to

[18] 100,000 Tons ("M")

713M tons in 1971. The [18]increase is equivalent to about four fully [CX 26D] developed Johnsonville-type process lines. Even if growth should fall short of these expectations, any reasonable projection will require major expansion in the industry. *It is believed that Pigments Department has the technology, the operating and construction capability, the cash generation capacity, and the waste disposal expertise to capture the major portion of this market growth. If this be true, there is the potential to increase market share from the current level of 31–32% to 56% by 1980, and with the trends persisting to approach 65% by 1985.*

A program designed to seize this opportunity would have specific implications, all of which would have to be resolved quantitatively at as early a stage as possible.

Adoption of a pricing policy which would provide adequate profit and cash generation for expansion.

Decision on configuration of production facilities. It seems obvious that within this time period a fully developed third site would be necessary.

A substantial increase in our commitments for titanium mineral. There appear to be adequate possibilities for large-scale ilmenite supply.

Final decision between waste disposal alternatives including beneficiation of ore, electrolysis or ferric chloride oxidation.

A program to acquire and train about 200 exempt salary personnel by 1977 [CX 26E].

* * * * * * *

In summary, Pigments Department finds itself in a unique situation. In technology, it is in a position of undisputed leadership not only in this country but in the world. Although the ability to use low grade ores in the chloride process has been known since 1950, no other producer has been able to achieve this capability. Most producers have directed their technical programs toward developing a beneficiated ilmenite which, at best, would show economics similar to rutile. In scale, [19]*Pigments Department is the only producer with large units which permit holding unit capital investment at lowlevels.* We are not aware of any other producer with waste disposal technology which can be accomplished without severe economic penalty. These same considerations apply to operations in foreign markets and separate studies to define the Department's participation in these markets are underway.

It is recommended that agreement in principle be granted to the Department to proceed with full development of this program. It is anticipated that substantial additional information will be provided in the Annual Report to be submitted in November 1972. In [CX 26F] succession, appropriation requests requesting authorization of the expenditures necessary to provide the required facilities will provide your Committee with the detailed considerations necessary for your evaluation of each step prior to the authorization of the capital funds required [CX 26G emphasis added].

27. In an "Advice of Action" addressed to Mr. Geil and dated May 31, 1972, the Secretary of the Executive Committee advised [CX 27A]:

Referring to your report dated May 25, 1972, on above subject [Opportunities in the TiO_2 Business]:

After discussion with you, J. H. Baird, Assistant General Manager, C. I. Smith, Jr., Director, R. A. Hageman, Manager, Plants Technical, Production Division, J. E.

Kramer, Director, Sales Division, Pigments Department, R. E. Manning, General Counsel, C. E. Welch, Assistant General Counsel, R. J. Reichert, Manager, Environmental Control, Government Affairs and Tax Division, Legal Department, and E. F. Ruppe, Director of Environmental Affairs, it was moved and unanimously carried that the Executive Committee agrees in principle with the program presented in the above-mentioned report, and grants authority to Pigments Department to proceed with full development of this program.

28. On June 20, 1972, J. E. Kramer, Director, Sales Division, Pigments Department, forwarded to J. H. Baird, Assistant General Manager, a recommendation by H. C. Ballard that DuPont not increase its TiO_2 pigment prices. Kerr-McGee had announced a 2¢ per pound price increase on rutile TiO_2, effective July 1, [20]1972. In addition to the reasons stated by Ballard,[19] Kramer stated (CX 28A):

. . . A price increase would markedly improve our competitors' economics and permit them to expand production facilities and increase share of market.

Attached to the Kramer memorandum was an in-depth analysis of competitive earnings at certain price levels including the current prices at 1¢ and 2¢ price increases (CX 28E). DuPont did not increase its prices and Kerr-McGee reduced its increase to 1¢, thus creating a "two tiered" pricing situation (see CX 70C).

29. On July 12, 1972, the Executive Committee approved the Pigment Department's Authorization request for the expansion of the New Johnsonville plant from 141M to 196M tons per year (CX 29). The Pigments Department reported that this appropriation was for the accelerated expansion program for New Johnsonville spelled out in the 1972 White Paper, i.e., CX 26 (CX 29D, E).

30. In the Pigment Department's Annual Report for 1972 (November), it reported to the Executive Committee that other producers appeared to be unable to expand due to problems associated with small-scale chloride plants needing high grade titanium mineral, waste disposal and lacking advantage of scale and sulfate plants requiring extra processing steps to meet chloride quality and uncertainties with respect to disposal of a large volume of pollutants produced by the sulfate process (CX 34, G, H). The report reiterated the 1972 White Paper objective, including the "adoption of a pricing policy providing adequate profit and cash generation for expansion" (CX 34 I).

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[19] The reasons given by Ballard were that most of the large customers were "price protected" through the end of 1972 and that any price increase would affect the small customer. Moreover, this price raise, following a substantial price increase in late 1971, could be in conflict with the Economic Stabilization Act of 1970 and might be considered "gouging" by the trade. Another reason was that Kerr-McGee and G&W were selling TiO_2 pigments at prices lower than DuPont's list price. Ballard stated: "Maintenance of present prices would appear, for the near future at least, to permit a respectable return on investment and adequate generation of cash for expansion" (CX 28C, D).

31. In November 1972, the Pigments Department advised the Executive Committee in connection with a study of foreign TiO_2 opportunities that, although it had received a large number of inquiries with respect to the purchase of manufacturing rights to DuPont's unique technology and proprietary expertise, with the exception of the construction of the high grade rutile chloride plant for Sherwin Williams, it had confined itself to DuPont's domestic expansion, conversion of a Mexican sulfate plant to the chloride process and construction of a plant in Argentina (CX 33C). [21]

32. In connection with an ongoing study of the feasibility of DuPont's entering the TiO_2 pigments market in Europe, A. H. Geil, in a discussion with the Executive Committee on July 18, 1973 (CX 38), indicated that the reasons supporting construction of 110M and 220M tons per year production lines at Brunswick, Georgia[20] to start up in 1977 and 1979, respectively (CX 38 L, W), and a 110M ton per year plant in Europe were (1) DuPont's advantage of technology and scale and ability to assume leadership in innovation, quality, service, and price and (2) the developing shortage of TiO_2 pigment. As to the latter reason, it was observed: "If we don't step into the breach and build capacity, one or more of our competitors will" (CX 38C). This document contains a summary of domestic TiO_2 competitors and DuPont's perception of their expansion plans (CX 38F).

33. On November 7, 1973, DuPont announced by corporate news release through its Public Affairs Department that it planned to build a TiO_2 pigments plant at De Lisle, Mississippi, to start operation by 1977. The press release stated that the De Lisle plant would be built with expansion in mind (CX 159 H, I). In this respect the statement reads:

> As the plant expanded additional employment opportunities would be created and ultimately it might employ between 1,000 and 1,200 persons. Expansion would depend upon continued growth of the markets for titanium dioxide . . . . [CX 159 I].[21]

34. In its 1973 Annual Report to the Executive Committee, the Pigments Department reported that plans were "well under way to exploit the Department's strengths in the chloride process in both the domestic and European markets" (CX 40C):

> . . . The Department continues to capitalize on its position as the lowest cost producer by expanding capacity at the New Johnsonville, Tennessee, and Edge Moor, Delaware, plants. Programs are being developed for the start-up of large, new plants in the United States (1977) and Europe (1978).

[20] Although the site of "Plant X", mentioned in the 1972 White Paper, was first chosen as Brunswick, Georgia, local environmental considerations required the shift of locale to De Lisle, Mississippi (See tr 1035–36 (Baird)).

[21] The last sentence of the statement reads: "The plant at Wilmington [Edge Moor] . . . currently is being converted to the chloride method in a major expansion."

35. On December 6, 1973, the Pigments Department presented its appropriation request (Part 3) for funds to complete the expansion of the New Johnsonville plant to 228M tons per year. In this request, it reported that the shutdown of the PPG chloride plant and NL's shutdown of its rutile chloride process plant and part of its St. Louis sulfate process plant plus the [22]curtailment of foreign imports had removed approximately 150M tons of finished TiO_2 from the domestic market and had created a severe industry-wide shortage. Due to favorable economics resulting from these circumstances, DuPont changed its plan to close down its higher cost operation at Antioch. The appropriation request was approved by the Executive Committee on December 12, 1974 (CX 41A).

36. In February 1974, DuPont turned down a request by NL for a license for its ilmenite chloride technology (CX 3 ## 136, 137; CXs 44C, D; 46A, D).

37. On March 27, 1974, the Executive Committee approved the Pigment Department's appropriation (Part 3) request for funds with which to complete the conversion and expansion of the Edge Moor plant to 167M tons per year capacity (CX 49). In its request, the Pigment Department stated (CX 49 G):

> The market for titanium pigments has been continuously growing while industry capacity has been relatively stagnant, forcing allocation during the past two years. This coupled with rising raw material, labor and pollution abatement costs for the industry has accelerated selling prices beyond that forecast in the Part 2 [appropriation request]. Now that the Phase IV price controls have been modified on titanium pigments an additional increase of at least 3.5¢ per pound is expected almost immediately and thereafter an increase of about 1.75¢ per year. For comparison, the unit sales price expected in the third year of this project is $36.77 per cwt. versus $26.43 used in the Part 2 calculation (1Q-1974 rate is about $28/cwt.). Because of the Department's advantages over competition—market knowledge, advantages of scale, advanced chloride technology, ability to use lower cost ilmenite ore and development of practical waste disposal schemes—the selling price increases will more than offset the anticipated higher costs. As a result, DuPont's titanium dioxide profit margin will return to or exceed historical levels and the return for this project increases accordingly.

38. On July 10, 1974, the Executive Committee approved the Pigment Department's first appropriation request (Part 1) for $8 million for "partial design, preparation of a current appraisal suitable for full funds authorization and cancellation charges on long-term delivery equipment" at the proposed De Lisle plant (CX 54A). In its appropriation request, the Pigment Department reported on the expansion projects at the three operational TiO_2 plants—Antioch (30M annual tons) Edge Moor 1 (167M annual tons) and New Johnsonville (252M annual tons)—and added "when these

expansions are complete in 1977, capacities at these sites will be at their desired practical limits" (CX [23]54C). The request goes on to reiterate:

> The market for titanium pigments has been continually growing while industry capacity has been relatively stagnant, forcing allocation during the past two years. The opportunity now exists for DuPont with its marketing knowledge and technology to launch a major expansion program. This will require development of a new plant site. [CX 54C]

39. On July 16, 1974, DuPont issued a press release on the De Lisle project. This press release stated that this plant, scheduled to begin operations in 1977, was planned with further expansion in mind. The press release also reviewed the expansion under way at Edge Moor and New Johnsonville (CX 159 F, G).

40. In early 1975, DuPont's competitors announced a 5¢ price increase. DuPont did not raise its prices and its competitors' price increases were rescinded (see CX 201A).

41. In 1975, due to the precipitous downturn in business in late 1974 (See CX 71F), the Pigments Department Task Force undertook a reexamination of the TiO_2 growth strategy outlined in the 1972 White Paper (CX 73A). K. H. Quisel and R. L. Heffelfinger stated that the current (1975) strategy was, among other things, fast growth from 1976 to 1980 and to obtain a 52–55% share of the domestic TiO_2 pigment market. It was thought that "as long as DuPont is aggressive, only U. S. expansion will be Kerr-McGee's 50M tons per year plant." This was attributed to "high waste disposal costs, low cash for some, and inability to build large plants." As to price, it was thought that a 3¢ per pound per year increase would yield the necessary return for De Lisle and also give competition generally adequate return to stay in business (CX 76A, B).[22]

42. On July 15, 1975, DuPont announced a 3.5% price increase on its TiO_2 pigments, which was immediately followed by its competitors, effective in early August (CXs 78; see CX 161C, CX [24]201; RX 2).

43. In the summer of 1975, Pigment Department's task force engaged in an in-depth analysis of the TiO_2 business, the evolution of DuPont's market strategies and detailed projections on various alternative business plans (See CX 85A, B, 91, 92). The completion of

[22] In summarizing the major "changing points" in TiO_2 strategy it was observed (CX 76D):

> *Price*
> In 1972, strategy appears to have been to maintain prices at a point to provide cash for DuPont expansion, but limit competition's ability to expand.
> Price forecasts have gradually increased as magnitude of new JV, EM, and De Lisle investments became apparent.
> Current pricing forecast should keep competition in business without enough cash to expand.

this study was accelerated when the Executive Committee called for a reappraisal of certain investment projects including the De Lisle project.[23]

44. On October 10, 1975, the Pigment Department made a presentation to the Executive Committee to justify continuation and completion of the De Lisle project (CX 116). The presentation compared four alternatives: (1) the proposed De Lisle program ("De Lisle"); (2) an alternative program that would provide the maximum reasonable time deferral of the proposed De Lisle program and its potential consequences ("Delay"); (3) an alternative program, if any, that would be accomplished at less cost, and the consequences thereof, ("Maintain Share"); and (4) the consequences of essentially abandoning all expansion programs ("No Expansion").

In connection with the De Lisle proposal, the Pigment Department, after reporting on DuPont's unique cost advantages over its competitors[24] stated (CX 116 G, H, I, J):

* * * * * * *

The second half of the reason for this TiO_2 program concerns TIMING.

In 1971 and 1972, DuPont launched a program to aggressively gain a commanding position in the market place. This program has been going according to plan. On this *FIFTH CHART* are listed reasons why now, as a result of that plan, is a unique point in time for our TiO_2 business.[25] [25]

We are the lowest cost producer in the world. A major part of this is based on low-grade ore and on scale of operation. We estimate that in ten years competitors will have solved these problems, particularly if they are encouraged to expand.

We have publicized through the various press releases and speeches of Company officials that we plan to expand. This has made us into the most-favored supplier in the eyes of customers who depended upon us in the last shortage and are planning on our covering them in the next shortage. If we drop out of this leadership position by cancelling De Lisle we foresee we will lose some of our position as most-favored supplier.

Because the big accounts must depend upon us as their major supplier, they also depend upon us to develop products which meet their needs. The way this has been carried out is that each new grade is generally developed with one or more big accounts. This cuts the lag time on grade introduction to almost zero. If we lose our credibility with these accounts [CX 116 H] by cancelling De Lisle, we will lose at least a part of this special product development relationship.

One of our major strengths lies in the ability to operate large-scale plants. This

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[23] Due to a general business slowdown following the oil embargo, and a tight cash flow position, DuPont found it necessary to curtail certain investment projects. On October 10, 1975, it heard approximately 10 reports relating to projects which had theretofore been deemed to be neither expendable nor nonexpendable (Category 3). In effect, the Pigment Department's De Lisle project was competing with other projects for the limited investment funds available (tr 711–717 (Shapiro); RX 16).

[24] "The most significant points are chloride is cheaper than sulfate; large chloride plants are cheaper than small; and DuPont has at least a 5¢ (and frequently much larger) advantage over its competitors" (CX 116 G).

[25] "TiO_2 strategy; Unique Point in Time; Lowest Cost Producer; Customers Expect Expansion; Product Development Enhanced by Leadership; Market Will Support a Big Plant Now But Not Later; New Site Has Value; Market Share Has Value" (CX 116U).

gives us significant cost advantages. This advantage, however, incurs large capital outlays when a major expansion is undertaken. This means the plant must be operating at a high rate within 3–4 years to be economically viable.

TiO_2 sales quantities have long followed GNP and Pigments and the Economist's office feel this relationship will continue during the period for which we are strategizing. Over this time, we expect TiO_2 use in the U.S. to grow at better than 5% (while the recovery is returning us to the long-term trend line), but then drop to about 2.7% in the 1980's. This means that in the immediate future we can fill a De Lisle in a little over three years; whereas by the end of this period, filling such a large plant will take about five years.

A new site has value to Pigments. Pigments now has a very large portion of its production for the paint [CX 116I] industry concentrated at Johnsonville. De Lisle would help minimize for our customers the risk of any kind of disturbance that was local in nature. Delays at De Lisle continuously increase our vulnerability to [26] opposition in obtaining permits. If we delay by about three years from our original 1975 funding, we will have lost our current political support and, with it, our ability to keep permits active.

Market share has value to us. In capitalizing on our strengths, we will increase our share. [CX 116 J]

With respect to the "Delay" alternative, Pigments reported that "a one-year additional delay in funding to 1977 represents the maximum time delay," the principal disadvantage being lost sales and earnings (CX 116 J).

With respect to the "Maintain Share" alternative, the Pigments Department outlined its considerations to alter some plans for completing Edge Moor to keep DuPont's grade structure in balance with the market and a "reamout" at Johnsonville, increasing capacity to 252M tons per year. (For an explanation of the term "reamout" see tr 1084 (Baird)). It concluded (CX 116M):

In the market place, as soon as it would become clear that DuPont had abandoned De Lisle, we would expect to see an additional price increase of about $2/cwt above our preferred case ["De Lisle"]. In addition, we would expect Kerr-McGee to build the plant they announced at Mobile but haven't started. We would also expect several others to expand. This might well be American Cyanamid and Glidden who have both told customers they would like to expand but haven't moved yet, apparently because of the pricing situation. When these expansions start up about 1980, we would expect a temporary oversupply which would cause some erosion of prices, so that by about 1982 we would expect to see the price drop about $2/cwt below the base case price structure.

Finally, with respect to the "No Expansion" alternative, the Pigment Department stated (CX 116N):

Abandoning the TiO_2 expansion program would mean simply maintaining the three existing plants. During our strategy re-analysis, we did not give this case the finely structured study that we gave the other cases. For purposes of this presentation, we've assumed that our plants would fill rapidly and stay full. We've also assumed

pricing equal to the previous alternative. In fact, this is probably overly optimistic because badly-timed expansions would probably periodically cause erosion of prices.

The Pigment Department summed up its presentation as follows (CX 116"O"): [27]

In summary, TiO_2 offers DuPont a low risk, high return business opportunity . . . [i]t is noteworthy that Reports on Accomplishment for TiO_2 projects over the last ten years have averaged 112% of forecast.

45. In its Annual Report to the Executive Committee dated December 1, 1975, the Pigments Department stated in pertinent part, with respect to its TiO_2 business (CX 120 Q):

Business Description

. . . In spite of shortages in 1973–1974, only DuPont and Kerr-McGee have indicated plans for major expansions. DuPont's business is strongly focused on domestic markets where it is the undisputed leader because of superior manufacturing technology; lowest costs; good protection in titanium ore, a major raw material; experience and resources to respond rapidly to market opportunities; and a 41% market share.

Business Objective and Financial Goals (1975–1980)

The business objective is to complete implementation of the growth program outlined to the Executive Committee in the Department's report of May 25, 1972. This is, in essence, to exploit a unique opportunity to capture most of the domestic industry growth into the early eighties, thus increasing market share above 52% and operative earnings to about $200MM per year.

General Business Strategy

The strategic plan to implement the growth program capitalizes on the internal strengths and competitive factors which have yielded DuPont a position of leadership. Key elements are:

Start-up new facilities at De Lisle, Mississippi, in 1978. This expansion, as the recently completed ones at Johnsonville and Edge Moor, exploits the ability to operate large scale plants utilizing low grade, lower cost titanium ore.

Continuation of process innovation and improvement programs to maintain position as lowest cost producer. This work will affect both the product line and the development of new, more unique products. For example, the De Lisle design incorporates new lower cost (both manufacturing and investment) finishing technology. [28]

A pricing policy to bring operative margins to 25–35%. Prices are forecast to increase about 6% annually; assessments of competitor's costs indicate this is consistent with price increases they will require to recover increasing costs of ore and waste disposal.

Continued focus on domestic opportunities . . . In addition there are world wide opportunities to license DuPont's chloride technology, capitalizing on it while it is still valuable to generate additional cash flow.

46. In early 1976, after NL and Cyanamid announced a 4¢ per pound price rise on rutile grades, of TiO_2 and a 3¢ per pound increase on anatase, DuPont announced a 3¢ price rise on all products and all

competitors adjusted their prices to match DuPont's (CXs 200A, 201A). R. J. Fahl, stated in a memorandum to J. E. Kramer proposing the 3¢ increase, that this increase "would not shrink the market significantly and would permit our projected market growth and penetration to continue" (CX 200A).

47. On June 16, 1976, the Executive Committee approved the Pigments Department's appropriation request (Part 3) for funds to return the De Lisle project schedule to a first quarter, 1979, turnover, for visible site preparation, and an expansion of the proposed plant from 130M to 150M tons per year (CX 133). Based upon an analysis of competitive capabilities to expand versus DuPont, Pigments Department reported (CX 133M):

> Analysis of cost and investment data indicates that most competitors are operating at a disadvantage versus DuPont and that a major expansion by them would be financially marginal, particularly if DuPont proceeds with De Lisle. The one possible exception is Kerr-McGee which now has an estimated 6% of the industry capacity. Earlier they announced a 50M tons-per-year pigment expansion and a 100M tons-per-year beneficiated ore facility to be located near Mobile, Alabama. Construction has started on the beneficiation plant, but the pigments expansion was postponed indefinitely in October 1975. *It is expected that their expansion plans will be determined largely by the rate of recovery of the TiO_2-consuming industries and by their estimate of additional market share available which could be influenced by DuPont's announced plans and visible actions at De Lisle.* We believe it unlikely they will have additional capacity before 1980. In our industry capacity forecasts, we have assumed they will have a 50M tons per year plant operating in 1981 [Emphasis supplied]. [29]

As to selling price trends, the Pigments Department stated (CX 133M, N):

> Industry selling prices were increased by 3.5¢ per pound (9%) in August 1975, even though the industry was operating at only 70% of capacity, and again by 3¢ per pound (7%) in March 1976. These increases were above those forecast in the Part 2 [appropriation request]. In our discussions with customers, we have been candid relating the need to increase prices to maintain our expansion activities and their acceptance of the recent price increases is indicative of their understanding of the impact of increased costs.
>
> Prices are forecast to increase 5–7% annually from current levels through the early 1980's. Several elements are at work to sustain these rates of increases. We estimate the inflation in the general economy [CX 133M] coupled with more stringent pollution control requirements will force competitive costs up about 8% per year over the next several years. The old sulfate plants cannot be expected to achieve productivity increases to offset these increased costs. Selling prices for project return purposes are considered to be conservative estimates because they do not allow for full recapture of estimated competitive cost increases of the sulfate producers by as much as two cents per pound. *The high investment cost required to provide additional capacity should prevent overcapacity developing to depress prices* [*Emphasis supplied*].

48. On June 21, 1976, DuPont issued a press release on the

authorization of the $20 million additional for the 150M ton per year TiO_2 plant it expected to begin building at De Lisle in 1977, and have operating by 1979. Although pointing out that the 1979 start-up was two years behind the original schedule, the press release reported that DuPont had said in early 1975 "it would pace construction to the recovery in the economy following the downturn which began in the fourth quarter of 1974" (CX 159 B).

49. On November 10, 1976, the Executive Committee approved the Pigments Department's appropriation request (Part 4) for funds to complete the expansion *of* Edge Moor including the installation of Simultaneous Drying and Grinding equipment (CX 198 B–E, I).

50. On March 23, 1977, the Executive Committee approved (CX 158A, 198A) the Pigments Department's appropriation request (Part 4) for full funding of the De Lisle project. Concerning competitors' capabilities to expand versus DuPont, the Pigments Department reported (CX 158N, O): [30]

Kerr-McGee remains the only competitor to announce a major expansion to start up before 1981. They planned to build a 50M tons per year TiO_2 plant at Mobile, Alabama with a 100M tons per year ore [CX 158N *in camera*] beneficiation plant at the same site. The beneficiated ore was to supply both their new plant and the existing Hamilton, Mississippi plant. Their ore beneficiation plant started up last year, and is expected to be at normal operating rates by this spring. *Our competitive cost-analysis program shows it would be financially more profitable for them to sell the beneficiated ore than to build a plant to convert it to TiO_2 pigment.* We believe the earliest they could start up a chloride line would be 1980 and have included this in our capacity forecasts.

NL Industries has announced plans to start up a chloride plant in the early 1980s, after the technology has been developed in Germany. If this plant is built, we believe it will replace their Sayreville, New Jersey sulfate plant, which was the highest cost domestic line, and was shut down from February 1976 to February 1977 because of a bitter strike. Their permit to barge acidic waste to the ocean expires in 1981.

The five domestic sulfate plants (which provided over 60% of 1976 competitive capacity) dispose of their acidic waste as follows:

Plant	*Disposal Method*
NL-St. Louis	River discharge
NL-Sayreville	Ocean dumping
American Cyanamid-Savannah	Neutralization-gypsum manufacture
SCM-Baltimore	Neutralization-river discharge
Gulf & Western-Gloucester	River discharge

No environmentally sound, economical way to handle these wastes has been developed. As pollution regulations become more strict, these plants will face rapidly increasing costs. The NL-St. Louis plant was sued by the federal government in January because it did not build a treatment plant for its acidic discharges, as required by the current EPA permit. The suit seeks daily fines of $10,000 until the treatment plant is operating and more than $400,000 for past pollution. We believe

sulfate plant shutdowns are more likely than any [31]additional expansions [Emphasis supplied].[26]

51. On April 4, 1977, DuPont announced the authorization of more than $110 million in additional funds to continue construction of the De Lisle plant. DuPont stated that the plant was expected to be operational in 1979 (CX 159A).

52. In May 1977, SCM and NL announced 5¢ per pound price increases on TiO_2 pigments. Shortly thereafter DuPont raised its prices 2¢ per pound and its competitors' rescinded their 5¢ price increases and matched DuPont's new price (see CX 161–166F).

In a memorandum to A. H. Geil and J. H. Baird dated May 6, 1977, J. E. Kramer stated that the rationale for a 2¢/lb. increase vis-a-vis 5¢/lb. was as follows (CX 163A):

Unit cost of manufacture have and are projected to increase only 2.2¢/lb between 3/76 and 3/78 while selling price will have increased 5¢/lb.
Worldwide imbalance of supply and demand estimated to be + 350,000T. High prices would invite off shore producers to have larger U.S. market share.
Reverse downward trend of market share; we do not need De Lisle if we can not capture market growth.
Deterrent for further reduction of TiO_2 in end use products.
Smaller price increases more palatable to our customers and can be more readily passed on to customer [Emphasis supplied].

53. In its 1977 Annual Report to the Executive Committee, dated December 5, 1977, the Pigments Department reported the following pertinent information relating to its TiO_2 pigment business (CX 196F, G, H, W):

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[32]*The domestic titanium dioxide pigment (TiO_2) business has been experiencing increasing problems of oversupply and price-discounting.* The principal contributor is the continuing sluggish recovery of the European and third-world economies. This is encouraging a number of foreign producers to export to the United States at below market prices and in volumes estimated to be 62% ahead of last year. *Softening domestic demand is aggravating the situation.*

In spite of these problems, the TiO_2 business is expected to achieve record sales volumes and pretax earnings in 1977. *Based on government data and reports from customers, it appears several of the larger domestic producers have been more adversely affected by the imports with sales significantly below 1973 levels. Our cost estimates indicate they may be operating at break-even or worse.*

The situation has caused the forecast achievement of prices and volumes presented in the De Lisle project to be one year behind schedule. A price increase of two cents to 48.5 cents per pound for bagged rutile pigment announced around mid-year will not

[26] In analyzing the possible sales forecasts, the Pigments Department states: "Shutdown of a single domestic manufacturing unit, or the failure of Kerr-McGee to follow through on its announced expansion plans, would increase DuPont's sales comparable to the increased demand [as forecast in the most optimistic economic conditions] (CX 158R).

become fully effective until the end of the year. Prices in Europe are equally sluggish running five to eight cents less than U.S. prices. [CX 196F *in camera*]

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DuPont remains the only TiO_2 producer pursuing an active expansion program. Trade comments would indicate several domestic competitors may be having profitability and environmental compliance problems which could lead to capacity reductions.

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The current sluggishness of the TiO_2 business should not delay the De Lisle construction activities. A delay would have minimal effect on cash flow as $140MM (of $182MM authorized) has been expended or committed. Even under the pessimistic assumption that sales volume and prices slide two years versus project projections, the TiO_2 business would still break even in 1979 (the start-up year) . . . . [CX 196G].

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A better choice is continuation of construction in the most economical way (e.g. no overtime or additional hiring to make up [33]construction delays), leaving the option of temporary mothballing at time of completion. This approach could delay start-up now scheduled for the first quarter of 1979, by at least one to two quarters. Further study by Engineering will provide more definitive schedule information by mid-December. This construction route offers the advantage of having the plant available to meet a sudden surge of demand brought about by a turn around in the world economic situation or by removal of TiO_2 capacity from the market due to competitive environmental or profitability pressures. [CX 196H]

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The business objective is to complete implementation of the growth strategy and program outlined to the Executive Committee in the Department's report of May 25, 1972. This is, in essence, to capitalize on a unique opportunity to capture most of the domestic growth into the early eighties, thus increasing market share above 51% and operative earnings to almost $150MM per year by 1982 [CX 196W; Emphasis supplied].

54. The cost advantage that DuPont has over its competitors has several parts. DuPont is the only TiO_2 manufacturer that has built and operates large scale, low grade ore, ilmenite chloride process plants (see CX 40F-G). This gives DuPont the advantage of sale economies as well as an advantage in lower plant investment costs (see CX 3 ## 20, 21; CX 61). In addition, ilmenite ore is much less expensive than the rutile ore or beneficiated ilmenite (synthetic rutile) used by its competitors who operate rutile chloride process plants. The waste disposal costs of a chloride process plant are lower than the waste disposal costs of sulfate plants (CXs 40G, H; 51). The high grade ore chloride plants have some cost advantages over the low grade ore chloride plants in that they use less chlorine gas per ton of TiO_2 produced and create less waste per ton of TiO_2 produced (see tr 1341–44 (Clark)).

In order for competitors to eliminate or reduce substantially DuPont's cost advantage in the manufacture of TiO_2 they would have to develop a low grade ore technology and build large scale chloride process plants (tr 1390–91 (Clark); CXs 23, 116H). The record shows that development of this advanced technology at large scale entails a substantial learning time (tr 1386–87 (Clark)). DuPont estimates that it would take from 5 to 10 years for a competitor to come close to DuPont's cost of production (CX 116H; see 1387–89, 1434–35 (Clark)).

The general nature of DuPont's cost advantage (including the estimated costs for De Lisle) is demonstrated graphically in [34]a chart that appeared in the Pigments Department's Part 3 appropriation request for funding of the De Lisle project (CX 133L) (Appendix F).[27]

DuPont's cost advantage became pronounced in the early 1970's and increased until at least 1972 as the price of rutile ore increased dramatically due to a shortage in that raw material. In addition, beginning in the early 1970's, sulfate manufacturers have faced very high costs of waste disposal. NL completely closed down its sulfate plant in St. Louis because of its inability to meet the environmental requirements as to the disposal of its waste.

The record shows that DuPont's cost advantage has decreased recently primarily due to an increase in the price of chlorine, a high energy product (CX 76D). However, DuPont has predicted that its cost advantage will exist for the foreseeable future (CX 209K–Z, *in camera*).

55. In the 1972 White Paper, DuPont adopted a "pricing policy" which would provide adequate profit and cash generation for expansion (CX 26E). From May 1972 to June 1978 there were 12 announcements of TiO_2 list price increases, and DuPont either led or met fully the announcements by competitors on eight of those occasions (CXs 3 ##194–235, CX 166).

In June 1972, shortly after DuPont began its growth "strategy," Kerr-McGee announced a 2¢/lb. price increase on rutile TiO_2. SCM and NL then announced a 1¢/lb. list price increase. DuPont and G&W did not raise their prices and Kerr-McGee lowered its price increase to 1¢/lb. This resulted in an unusual two tiered pricing structure in the TiO_2 industry which apparently lasted until 1974 when "price controls" were removed (see CXs 28A, C; tr 886–890 (Baird)).

[27] Similar charts appear in other DuPont documents, the first one appearing in CX 38T, in connection with a TiO_2 strategy presentation by the Pigments Department to the Executive Committee on July 18, 1973 (See also CX115F, 116T; 158N *in camera*). The record shows that at all times relevant to the issues in this case, DuPont has analysed its competitors' cost in detail (See CXs 23; 63; portions *in camera*; 64 portions *in camera*; 68L, "0"; 81 *in camera*; 82 *in camera*; 83 *in camera*; 98C *in camera*; 133M; 158N *in camera*; 196).

Many reasons were given for not raising DuPont's prices at that time. Although TiO_2 was in short supply, several TiO_2 producers and foreign importers were selling below DuPont's list price. Concern was registered about a price rise encouraging an increase in imports. In addition, many of DuPont's large customers had been "price protected," that is, guaranteed a certain price, until the end of 1972. There had been a substantial price increase at the end of 1971, and a [35]further increase, which would affect only smaller customers, could be considered "gouging" and might affect DuPont's "image as a preferred supplier." (CX 28B–D).[28]

In early 1974, upon the removal of "price controls," there were a series of four price increases which resulted in a total increase in the list price for rutile TiO_2 of approximately 12¢/lb. to a 40¢ level (CX 3 ## 196–99; tr 891–93 (Baird)). At one point during this period, DuPont was unsuccessful in its attempt to raise the price of its anatase TiO_2 by 5¢/lb., and it reduced this to 3¢/lb. to match competitors' lesser price increase (CX 3 ## 199–200; tr 892–93, 1208–09 (Baird)).

In January 1975, DuPont declined to follow several of its competitors' announced price increases of 5¢/lb. on rutile and anatase and the competitors' price increases were cancelled (CX 3 ## 201–04, 206–09; tr 894–96, (Baird)). Baird testified that by this time the effect of the mid-70's recession was being felt and that sales of TiO_2 had dropped substantially and that there was discounting from list prices by competitors (see RX 2C; tr 894–96 (Baird)).

However, in August 1975, DuPont led a 3.5¢/lb. increase in list prices, an increase that was followed by its competitors (CX 3 ## 210, 215; CXs 69, 78). The Pigments Department reported in pertinent part (RX 2C):

A 3-½¢/lb. increase is expected to restore earnings to a satisfactory level for the balance of 1975 and through the first half of 1976 in the absence of any unforecasted energy cost increase. Major customers have been advised informally that an 8–10% increase would be necessary soon, and appear willing to accept this level. Such an increase is in keeping with projected prices in the 1974 Annual Report and Supplement, and Project [36]2613, and is believed to be the best compromise level for restoring earnings without shrinking the market (customers will probably not undertake gross reformulation to use less TiO_2 if the increase is held below 10%). We believe all domestic competitors will rapidly follow this increase, as three of the six

[28] J. E. Kramer, in recommending that DuPont not increase its list price at that time, stated (CX 28A):

> A price increase would markedly improve our competitors' economics and permit them to expand production facilities and increase share of market. . . . In support of this we have heard two comments from our customers:
> PPG—Walter Ethier, Director of Purchases, PPG, stated that D. Benoit, Kerr-McGee District Manager, told him on 6/16/72 that Kerr-McGee had to raise prices 2¢ per pound in order to justify expansion plans.
> SCM—R. Lozon, Director of Purchases for the Glidden Durkee Division, told me that the TiO_2 industry should expand production capabilities. However, SCM could never justify expansion facilities at current prices.

attempted to initiate comparable increases in January 1975. Because demand at that time was so weak, we elected not to increase at that time.

During 1975, members of the TiO_2 task force, evaluating the growth strategy initiated in 1972, stated that:

In 1972, strategy *appears to have been* to maintain prices at a point to provide cash for DuPont expansion, but limit competitors' ability to expand. Price forecasts have gradually increased as magnitude of new JV, EM, and De Lisle investments became apparent. Current pricing forecast should keep competition in business without enough cash to expand [CX 76D, Emphasis added].[29]

In assessing DuPont's current strategy the task force stated: "Increase 3¢/lb./yr. to 1980 will yield necessary return for De Lisle based on current cost projections. Also give competition generally adequate return to stay in business" (CX 76B).[30] DuPont's officials testified that strategic pricing "was never used in our pricing" (tr 1248 (Clark); see also 889–90 (Baird)). [37]

In early 1976, NL announced an increase of 4¢/lb. on rutile TiO_2 and 3¢/lb. on anatase (see CX 129B). When DuPont raised its price only 3¢/lb. on both grades, NL lowered its price increase to 3¢/lb. on rutile. In his proposal for the 3¢/lb. increase by DuPont, R. J. Fahl stated his reasons (CX 129A):

This will represent an 10.8% increase (annualized) since August, 1975.
This places us one year ahead of the schedule reported in the Annual Report and De Lisle project submissions and provides operative earnings $14MM above forecast for calendar 1976 ($20MM annualized).
A 4¢ increase on rutile grades would penalize 84% of our current customers at the expense of the 16% who can utilize anatase. . . .
A 3¢ increase will minimize inroads by foreign competition. . . .
A 3¢ increase would be a clear demonstration of responsible pricing practices, and in line with projections on which customers have based their pricing policies. It would not shrink the market significantly, and would permit our projected market growth and penetration to continue.
A 3¢ increase will prevent further widening of the rutile/anatase differential. . . .

In May 1977, SCM and NL announced a list price increase of 5¢/lb. on anatase and rutile (CX 3 ## 226–29; CX 162A). DuPont declined to

[29] As a preface to their History of Reported TiO_2 Business Strategy, K. H. Quisel and R. L. Heffelfinger stated: "The key elements of the strategy have not been totally documented" (CX 76A).

[30] The task force directed the compilation of pricing forecasts that would show the following (CX 85B; CX 101A):

> Determine price which will trigger competitive expansions.
> Determine price where foreign competitive products will enter.
> Determine price where non TiO_2 products will substitute.
> Determine reaction of competitors to our strategy.
> Price that will cause any one to fold.

The Competition Situation Task Force filed a detailed report (CXs 100–05, 108).

match this 5¢ increase and instead announced a list price increase of 2¢/lb. Competitor's price increases were then rolled back to DuPont's level. J. E. Kramer's rationale for the 2¢/lb. increase instead of the 5¢/lb. increase was as follows (CX 162A):

The market is still not firm as there are many deals in all the industries we serve either by discounting price 3 to 4¢/pound, sale of "substandard" material at distressed price, or the use of extended terms. Through the first quarter, we sold 18% of our product at reduced prices as a result of meeting competitive action.
A worldwide supply and demand imbalance of ± 300,000 tons exists. Imports of titanium dioxide have increased during 1977 and substantially higher prices would invite offshore producers to have a larger U.S. market share.
A deterrent for customers to formulate their products to lower TiO_2 levels, and an incentive [38]for restoration toward historical levels. This is highly important to us, as our growth depends on an expanding market.
Smaller price increases are more palatable to our customers as they can pass the increases along easier.
Reverse downward trend of market share; we do not need De Lisle if we can not capture the market growth. When we aggressively priced from 1972 through 1975, we substantially gained market share even during the 1975 recession. From March, 1976 on we have not been aggressive in the market place from a pricing standpoint and as result, our market share eroded 2.5%.
Two cents per pound increase, effective June 1, 1977, and in place 100% by 11/1/77 is expected to yield additional earnings of $4.5MM during 1977.
Current average selling price is 44.9¢/pound and this increase should put us ahead of the price forecasted in both the Annual Report and Project 2613-14 (De Lisle) of 45.4¢/pound [emphasis supplied].

On January 23, 1978, R. J. Fahl recommended that DuPont roll back the 2¢ price increase of June, 1977. He stated (RX 7A):

The announced June, 1977 titanium dioxide price increase is not holding. I propose that we promptly announce that pre-June prices are in effect through the first quarter, and try to initiate an increase in the second quarter if conditions appear more favorable.

Thirty-eight percent of "TiPure" sales were at the current list price in December, but of this 38%, over 8% was as R-O (slip) codes or RPS with performance guarantees. In effect, 30% is conventional grades at current list, and the number of pricing actions we are asked to meet indicates this could drop below 25% by February.

Accordingly, it appears that DuPont's announced list prices during 1972 through 1977 were in the range where they generated enough cash flow to justify DuPont's expansion, and were too low to permit competitive expansion, although high enough to keep competitors in the TiO_2 business. It also appears that these prices were not artificially or unilaterally established by DuPont, but were controlled by the economic [39]conditions in the TiO_2 market (see CX 147C). These conditions were affected by "price controls", cost of inflation (especially energy costs), the severe recession of 1974-1975,

substantial excess supply of TiO_2, imports, and a reluctance of TiO_2 users to return to normal levels of use after a period where "reformulation" was prevalent (tr 1241–43, 1320 (Clark)).[31]

56. Immediately before DuPont adopted the growth strategy whereby it intended to capture the major portion of the expected growth in the domestic TiO_2 market, its total plant capacity was approximately 270,000 tons per year. The Antioch plant had a capacity of 28,000 tons per year; Edge Moor (sulphate) had a capacity of 55,000 tons per year; Edge Moor (chloride) had a capacity of 46,000 tons per year, and New Johnsonville had a capacity of 141,000 tons per year (see CX 15A–B). Its expansion plans for those plants were to replace the Edge Moor sulfate plant with a chloride plant of the same size (55,000 tons per year), to expand the New Johnsonville capacity to 196,000 tons per year, and to close the Antioch rutile ore plant (CX 15B, 21E, "O"). This would have resulted in a net gain in capacity of 27,000 tons per year by 1974. DuPont estimated that from this expanded capacity (approximately 400,000 tons per year) it would be able to supply demand for its TiO_2 until 1979–1981 before additional manufacturing facilities would be needed (CX 21K).

By May 1972, NL Industries had shut down its chloride plant at Sayreville, New Jersey, and PPG had abandoned its chloride plant in West Virginia. In addition, NL terminated its production of an extended TiO_2 pigment and the United States had imposed a 7.5% *ad valorem* duty on imported TiO_2 (see CX 21 H, I; 26C). This resulted in a shortage of TiO_2 in the domestic market.

In the 1972 White Paper, DuPont estimated that the projected growth in industry tonnage between 1972 and 1980 would be about 330,000 tons per year which was the equivalent (in 1972) to about three fully developed New Johnsonville-type process lines (CX 34H, I). After adoption of the program set forth in the 1972 White Paper, DuPont cancelled its plans to close down the Antioch plant and initiated plans to expand the New Johnsonville plant to 228,000 tons per year (CX 29D, K), to increase the capacity of the new chloride line at Edge Moor to 110,000 tons per year (CX 32D) and began plans to build two [40]production lines of 110,000 tons per year and 220,000 tons per year at plant site "X" (which eventually became the De

[31] Complaint counsel have proposed findings to the effect that DuPont in 1972 adopted, and have since engaged in, "a pricing policy which would provide adequate profit and cash generation for expansion but limit competitors' ability to expand," citing the 1972 White Paper (CX 26E), Kramer's recommendation on the June 1972 Kerr-McGee price increase (CX 28A), the Task Force's evaluation of the 1972 growth strategy (CX 76D), numerous Task Force documents disseminated throughout the company (CXs 113P, 114P), and similar Task Force statements in 1976 and 1977 (CXs 137C, 145D, 178) (See CXCPF 241–51). They also request a finding that DuPont implemented this strategic pricing policy when price roll backs were forced on competitors during 1975, 1976 and 1977 (See CSCPF 261). The record does not support such findings.

Lisle project) for an eventual capacity of approximately 750,000 tons per year by 1980.[32]

In November 1973, before the appropriation of any funds for the construction of De Lisle, DuPont announced its plans to build that TiO_2 plant (CX 159H, I). In May of 1974, Kerr-McGee announced its plan to build a 50,000 ton per year TiO_2 plant and a 100,000 ton per year beneficiation facility at Mobile, Alabama (CX 131I, K). In July of 1974, DuPont appropriated $8 million (of an estimated total of $165 million) to start the De Lisle project. At that time the Antioch plant had been expanded to a capacity of 30,000 tons per year and Edge Moor and New Johnsonville were being expanded to total site capacities of 167,000 tons per year and 252,000 tons per year respectively, those capacities being at the desirable practical limits (CX 54C). DuPont announced its plan to construct the De Lisle facility and the Edge Moor and Johnsonville expansions on July 16, 1974 (CX 159F, G).

Although Kerr-McGee built and started up its 100,000 ton per year beneficiation plant, it closed it in 1978. It has not yet started construction of the 50,000 ton per year TiO_2 plant at Mobile and DuPont no longer expects that it will go through with that construction in the near future. NL has announced that it will construct a 100,000 ton per year chloride plant, although construction of that plant has not begun.

Thus, except for DuPont, no TiO_2 producer has started construction of a new TiO_2 plant in the United States since 1970, and DuPont anticipates no such expansion in the foreseeable future.

An overall view of the growth of industry capacity and industry sales (including DuPont's forecasts to 1982) is demonstrated graphically in a chart that appeared in Exhibit CX 133I (Appendix G).

Although industry sales have not increased as expected since the 1974–1975 recession, some industry capacity was lost when NL closed its St. Louis sulfate plant in 1978 because of difficulties with pollution problems. NL has imported TiO_2 pigments to replace the supply lost by the shut down of the St. Louis plant. Other imports have remained at about 4% of domestic shipments (CX 223). Although total industry sales are [41]still at the 1972–1973 levels, DuPont's share of the domestic TiO_2 market increased from 30% in 1970 to approximately 41% in 1977.[33]

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[32] A comparison of DuPont's market share projections in February 1972 and July 1972 is graphically demonstrated on Appendix H (CX 21"0";29N;CSCPF p. 41).

[33] Complaint counsel have proposed a finding to the effect that DuPont's expansion of its TiO_2 capacity was not justified by market place conditions and that such over expansion was undertaken as part of a strategy to prevent its TiO_2 competitors from expanding their capacity. They also propose a finding to the effect that the DuPont press releases announcing the De Lisle project were exaggerated and were designed to affect competitors' decisions whether to expand their facilities. On this record, DuPont's proposed expansion was reasonably responsive to the

(Continued)

57. Before 1972, DuPont had received a large number of inquiries regarding the purchase of rights to DuPont's chloride technology, including requests from Cyanamid, Cabot, and Glidden (CXs 3, #127; 33C; 250C). All of these requests were turned down, except that DuPont constructed a rutile ore plant similar to its Antioch plant for Sherwin Williams (CXs 33C, 250D; tr 1386 (Clark)).

After 1972, DuPont has continued to receive inquiries on the licensing of its chloride process TiO_2 technology and has turned down such requests (CX 3, ## 132, 133). In 1974, DuPont turned down a request by NL for a license for its ilmenite chloride technology (CX 3, ## 136, 137, CX 45, CX 46D). This was not the first time that such a request from NL was denied (CX 3, # 138).

In connection with the NL request in early 1974, H.B. Clark, Manager of DuPont's TiO_2 Research & Development Department, recommended (CX 44C, D):

> National Lead has said they will buy the Sherwin Williams plant providing we will sell them the technology to use ilmenite in that plant. We should very clearly say no to this request. National Lead has the marketing base which could allow them with ilmenite chloride technology to deny us the sales that we require to make our new investments profitable.
>
> * * * * * * *
>
> It seems clear, however, that we should not wish to transfer our ilmenite technology to any major competitor (and very probably not even to Sherwin-Williams) since low cost ore and scale are the only two advantages we now enjoy and both of these are temporal. It would appear to me that the maximum gain from these two advantages will come from increasing our market share rather than collecting royalty payments or license fees from disseminating this information broadly. [42]

DuPont has considered license requests from foreign countries including Japan, Brazil, U.S.S.R. and the Peoples Republic of China, but has never completed any such negotiations (CXs 132C, 140D, 157, 180E, 188B; see CX 60).

Royalties for such licenses, especially domestic licensing of the lower cost ilmenite process, would have yielded substantial fees, a fact that has been considered by DuPont officials (see CXs 120Q, 157A–B).

Discussion

Section 5 of the Federal Trade Commission Act empowers the

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expected growth in demand for TiO_2. The record also shows that DuPont's announcements were necessary to inform the De Lisle, Mississippi, community, as to DuPont's plans as well as notify customers who were having difficulty obtaining TiO_2 in 1974, that DuPont intended to be a major supplier in the future (see CX 62F; 105A).

Federal Trade Commission to prohibit certain "unfair methods of competition" and certain "unfair or deceptive acts or practices."[34] Section 5 was intended to be a broad and flexible statute under which the Commission could designate as "unfair methods of competition" conduct that, although not previously deemed violative of statutes governing trade practices, had the anticompetitive effects that such legislation was designed to prevent. See H.R. Rep. No. 1142, 63d Cong., 2d Sess. 18–19 (1914). It is well settled that Section 5 covers conduct that either violates the prohibitions of the Clayton Act and the Sherman Act or conduct that could lead to unreasonable restraints on competition if not prohibited. See *Federal Trade Commission* v. *Brown Shoe,* 384 U.S. 316, 321 (1966); *Federal Trade Commission* v. *Cement Institute,* 333 U.S. 683 (1948).

An illegal attempt to monopolize constituting a violation of Section 2 of the Sherman Act involves a "specific intent" to control prices or destroy competition in a relevant market, predatory or anticompetitive conduct directed to accomplish those ends, and a dangerous probability of success. *Purex Corp.* v. *Procter & Gamble Co.,* 596 F.2d 881, 890 (9th Cir. 1979). *Janich Bros., Inc.* v. *American Distilling Co.,* 570 F.2d 848, 853 (9th Cir. 1977); *Golden Grain Macaroni Co.,* 78 FTC 63, 164 (1971), *enforced in part,* 472 F.2d 882 (9th Cir. 1972), *cert. denied,* 412 U.S. 918 (1973). It is generally accepted that monopoly power exists when an industry member has the power to raise prices or exclude competition when it so desires, and that such monopoly power is unlawful if it is willfully maintained or acquired as distinguished from arising from growth or [43]development as a consequence of a superior product, business acumen or historical accident. *Purex Corp.* v. *Procter & Gamble Co.,* 890 *supra; Golden Grain Macaroni Co., supra,* 78 FTC at 157.

Complaint counsel contend that DuPont had (and continues to have) the intent to prevent competition, to control prices and to gain a dominant share of the TiO_2 market. In this respect, complaint counsel allege that DuPont has engaged in certain strategic business conduct designed to perpetuate a so-called "investment asymmetry" between DuPont and its TiO_2 competitors, namely, the existence of business conditions under which competitors would not choose to construct large scale TiO_2 production facilities (CSCPF pp. 2–3, 96–98, 113–17, 123–25; see CX 218 pp. 43–44 (Shepherd); see also tr 1548–49 (Adelman)).

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[34] "Sec. 5(a)(1). Unfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce, are hereby declared unlawful.

"(2). The Commission is hereby empowered and directed to prevent persons, partnerships, or corporations, . . . from using unfair methods of competition in or affecting commerce and unfair or deceptive acts or practices in or affecting commerce."

Complaint counsel assert that as part of its strategy DuPont priced its TiO_2 products low enough to discourage competitors' expansion, yet high enough to fund DuPont's own expansion, engaged in premature expansion of its own TiO_2 facilities and capacity, made exaggerated announcements relating to its expansion plans, and refused to license its TiO_2 technology to its competitors. They contend that this exclusionary scheme was anticompetitive (CSCPF pp. 96–98, 120, 122, 124), and that through such strategy DuPont has insulated its substantial cost advantage from erosion over time. Complaint counsel contend that without large scale construction no competitor would be in a position to substantially reduce or eliminate DuPont's cost advantage through the necessary "learning by doing," inherent in the development of an ilmenite technology, or by scale economies, available from large chloride process plants. Complaint counsel contend that the intended effect of DuPont's strategy was to limit the funds available for competitive expansion, decrease the return that competitors could expect from expansion and increase the risks of such expansion (CSCPF pp. 2–3, 80, 86, 96–98). Complaint counsel conclude that if the results of this challenged course of conduct are not reversed DuPont will eventually obtain the power to raise prices or prevent competition at will (see CSCPF pp. 98–104, 113–17, 126–30).

Characterizing DuPont's challenged course of conduct as an "exclusionary growth strategy," complaint counsel take the position that such conduct violates Section 5 of the Federal Trade Commission Act because it constitutes an illegal attempt to monopolize the TiO_2 market violative of the Sherman Act, threatens an incipient violation of the Sherman Act, violates the spirit of the Act, and violates public policy insofar as it causes undue harm to competition, competitors or consumers (see CSCPF pp. 109–10, 123–25).

DuPont argues that there is nothing anticompetitive about an industry member attempting to gain market share and that such an "attempt" is the very substance of effective competition. It also contends that not one element of its challenged conduct [44]("growth strategy") is unlawful: that it did nothing illegal in obtaining its cost advantage over its competitors (see RespReply A7–A9); that its plant expansion and new construction were reasonable and necessary responses to anticipated increase in market demand for TiO_2 (see RespReply 6–7, A19–A24); and that it was under neither a legal nor a moral obligation to give its competitors (particularly NL) its ilmenite technology through licensing (see RespReply A24–A25). DuPont contends that its competitors had and continue to have the means and technical ability by which to develop their own ilmenite

technology or other low grade ore technology and their competitors' choice not to undertake the required investment in the past or present should not be held against DuPont (RespReply A25–A28).

DuPont claims that complaint counsel have made unwarranted assumptions about its growth strategy by attributing to DuPont's management certain policies that appeared in certain planning or analysis documents. For example, DuPont claims that it never engaged in the strategic pricing alleged by complaint counsel, that it did not forecast higher prices for TiO_2, should its growth plans prove successful (tr 1288–92, 1304, 1375–79, 1451–56, 1497–99 (Clark)) and that it never considered itself to have or to be able to obtain through its growth plans a monopoly share of the TiO_2 market (tr 1327–30, 1321–25, 1339–40 (Clark)). DuPont also claims that it never made announcements about its expansion plans that were not accurate and for a legitimate reason.

Although the record does not support complaint counsel's overall view of DuPont's growth strategy, it does support their view of the exclusionary effect of DuPont's expansion program on competitor's expansion, and the probability that DuPont will obtain substantial market (monopoly) power (see CSCPF pp. 104–09, 123–25; CX 218 pp. 7–9 (Shepherd)). There is no doubt that the Federal Trade Commission Act was designed to prevent unfair trade practices that have the tendency or capacity to create a monopoly or lessen competition. But in any proceeding brought under the Federal Trade Commission Act, the Commission, before it may issue orders deemed remedial or preventative, must find that a respondent's conduct constitutes an *unfair* method of competition or an *unfair* or *deceptive* act or practice.

No matter how DuPont's officials may have analyzed their future business opportunities that arose upon the advent of DuPont's substantial cost advantage in the early 1970's, and no matter how they have appraised the nature or effect of their growth strategy, I can find no *conduct* that can be considered "unfair" within the meaning of the Federal Trade Commission Act. Even complaint counsel do not assert that any individual action taken by DuPont, whether in acquiring its cost advantage, in its TiO_2 pricing, in its expansion of capacity or in its choice not to license its TiO_2 ilmenite technology was illegal or even unreasonable. Complaint counsel challenge the exclusionary *effect* of all of these actions taken together, along with their claim that DuPont *intended* such an exclusionary effect (see also CX 218 p. 27 (Shepherd)). [45]

In my opinion, the ultimate question in this matter is whether DuPont had *alternatives* to its aggressive growth strategy that it was

required to take, in lieu of the actions it did take, in order not to run afoul of the antitrust laws.

Dr. Shepherd testified that "DuPont should have done whatever it wanted to do, subject to the proviso that it not choose a strategy whose effect was to transform the TiO_2 industry into a virtual monopoly" (CX 218 pp. 65–66). In this respect Dr. Shepherd noted that DuPont had made analyses of various directions it could have taken (ibid). His testimony on the various elements of the strategy indicates that in his opinion DuPont should not have priced as low as it did or should not have embarked on such a large expansion program (especially the construction of the De Lisle facility). He was of the opinion that one alternative DuPont had was to license its ilmenite technology to its competitors (including NL) at some point in time after 1972.[35]

I am not convinced that DuPont was required to take actions different than those it did take. DuPont's cost advantage was the result of business foresight, intelligent planning, dedicated technological application to a most difficult production problem, the taking of economic risk, and its competitors' choice during the 1960's to build production facilities designed to use high-grade rutile ore. The development of the shortage of rutile ore and the advent of high costs of pollution abatement for TiO_2 producers were not accidental. Although DuPont's gain was not unexpected, the magnitude and the timing of this new cost advantage was unexpected. But this cost advantage was not "fortuitous" in the sense that it was either accidental or unearned.

I do not believe that DuPont was required to price its TiO_2 products high enough to insure its less efficient competitors sufficient revenue to finance expansion. The resulting higher cost of TiO_2 to user-customers (and ultimately to the consumer) and the resulting exorbitant profits to DuPont would be more antisocial in the long run than the natural exclusionary effect of the so-called "investment asymmetry" that developed in the TiO_2 industry before 1972. As detailed above (Finding 55), I do not believe that DuPont's [46]actual pricing in the period from May 1972 to 1978 could have been much different than it actually was, given price controls, the mid-70's recession and the slow recovery of the TiO_2 industry during 1976 and 1977 (see tr 1602–03 (Adelman)). In those situations where DuPont

[35] Dr. Shepherd testified (CX 218 pp. 66–67):

> I would like especially to consider another alternative that DuPont could have adopted—that of licensing its technology. DuPont had many opportunities to license its chloride technology. A policy which permitted licensing would have lowered production costs throughout the industry, while letting DuPont harvest extra profits in line with the cost savings made possible by its chloride technology. With licensing, the cost-saving benefits of DuPont's technology would not have been limited to its own production. . . .

failed to match its competitors' price raises, the market conditions did not justify such price increases. During the period 1975 to 1977 there was an over supply of TiO_2, producers were operating at approximately 70% of capacity, and there were substantial TiO_2 sales at prices discounted from list. If DuPont had raised its TiO_2 list prices substantially, and then sold at those prices, it would have placed itself at a competitive disadvantage and would have been considered a "price gouger" by customers.

The lowest cost producer's choice to expand capacity in a situation of short supply, is a sound business judgment that is economically justified. In 1973, when there was a severe shortage of TiO_2, DuPont was entirely justified in planning to build a new plant. The record shows that a plant the size of De Lisle was necessary to take advantage of scale economies. The record also shows that DuPont thought the future of the sulfate process plants was in doubt (tr 1443, 1510–11 (Clark)). Any theory that higher cost producers must be protected against the effects of expansion by their lower cost competitor is not sound economic theory. And certainly the construction of a plant at less than scale is not socially desirable. In the circumstances, the De Lisle expansion was a reasonable business choice in 1972, and was still a reasonable choice in 1975. DuPont's announcements of its plans for De Lisle were for legitimate reasons and were not necessarily for the purpose of restraining competitive expansion.

DuPont was not required to license its ilmenite technology to its competitors (or potential entrants, if any). The choice to look to long run profitability instead of immediate revenue from royalties is not unfair. There is no showing on this record that competitors could not develop that technology, if they had chosen to take that course of action. The fact that these competitors found themselves five to ten years behind DuPont in 1972 did not obligate DuPont to give up its technological advantage.

The final question is whether DuPont's course of conduct, neither unreasonable nor unfair, becomes unfair because DuPont, in forecasting the effects of its actions, i.e., limited or no competitive expansion and its own increase in market share, knew or should have known that it would acquire substantial market power. With knowledge that the success of its growth program depended on either minimal or no expansion by its competitors, DuPont nevertheless put a growth strategy into operation in 1972 and has continued that growth strategy to date. DuPont was aware that TiO_2 prices were low enough to discourage competitive expansion and acknowledged that increase in market share was important to its profitability. As the

dominant TiO_2 producer in the 1980's, DuPont predicted that it would be in a position to increase the profitability of that portion of its business in the foreseeable future. [47]

In other words, the question is whether DuPont was prohibited from engaging in any conduct, the *effect* of which might be to transform the TiO_2 industry into a virtual monopoly (see CX 218, p. 65 (Shepherd)). I do not think that business awareness of the nature of and the probable results of otherwise completely legitimate business conduct changes that conduct into an illegal anticompetitive practice or supplies an illegal intent to lessen competition or create a monopoly. I have found no prior "attempt to monopolize" case in the courts or before the Commission and not one has been cited by complaint counsel, that transforms lawful conduct into unlawful conduct without the presence of some overt or anticompetitive act considered unreasonable in the regular conduct of a competitive business.

I am not persuaded on the record considered as a whole that DuPont created, or unfairly maintained, the "investment asymmetry" which has existed in the TiO_2 industry since 1970 and which now is an effective barrier to the competitive expansion required by DuPont's competitors to place them in a position to challenge DuPont's impending dominance in the TiO_2 industry. Regardless of its market share, DuPont, in 1972, acquired the means to develop market power when it obtained a substantial cost advantage over its competitors. In my opinion whether DuPont adopted a less aggressive growth strategy program that complaint counsel and Dr. Shepherd appear to think it should have engaged in or the aggressive growth strategy challenged in this case, the so-called "investment asymmetry" would have nevertheless prevailed and the future prospects for effective competition would be just as tenuous as they appear today.[36] [48]

Section 5 of the Federal Trade Commission Act can be invoked to

[36] Dr. Shepherd was of the opinion that DuPont's behavior was that of a dominant firm and that its share of 40% of the TiO_2 market (where its nearest competitor's share was only 16%) indicates it already has substantial degree of monopoly power (see CX 218 pp. 7, 9). I do not agree that DuPont already has monopolized the TiO_2 market within the meaning of Section 2 of the Sherman Act. The record shows that DuPont does not have control over TiO_2 prices. It does not have the power to establish prices without regard to its competitors' pricing. However, when the De Lisle facility is in full production and the demand for TiO_2 increases as DuPont expects it will, a different case may appear. In this respect, Dr. Shepherd testified (CX 218 p. 8):

> . . . DuPont's market share seems to be likely to grow further, rather than suffer erosion. The record suggests that the sulfate TiO_2 plants now operating in the U. S. have a limited future. Meanwhile, DuPont has over 66 percent of all chloride-process TiO_2 production in the U. S. market, and this share will rise in the next year or two as the De Lisle plant opens. That plant, with up to 16 percent of U.S. TiO_2 capacity, will raise DuPont's total market share to at least 55 percent, and approximately 75 percent of the chloride-process TiO_2 production. Other producers have no major expansion under way, nor any present access to comparable chloride technology. Their sulfate-process plants are at an increasing cost disadvantage.

effect structural changes in an industry only where it is clearly demonstrated that the competitive disequilibrium is the result of some conduct that could be designated as "unfair". If the challenged conduct is not unreasonable and not the cause of the trend toward monopoly power, no violation of Section 5 exists, merely because the effects upon competition may be undesirable from an economic point of view.

Conclusion

I conclude that DuPont did not engage in the "strategy" attributed to it in the complaint and by complaint counsel in their proposed findings in that DuPont did not *engage* in "strategic pricing," but rather established its TiO_2 prices relative to market forces over which it had no control.

I also conclude that DuPont's conduct of its business, insofar as it is challenged in this proceeding, was neither unreasonable nor unfair and that its conduct did not constitute an illegal attempt to monopolize the domestic TiO_2 market in violation of Section 2 of the Sherman Act and did not constitute unfair methods of competition or unfair and deceptive acts or practices in violation of Section 5 of the Federal Trade Commission Act, as amended.

Order

It is ordered, That the complaint in Docket 9108, E.I. DuPont de Nemours & Company, is dismissed. [49]

Attachments:

Appendix A: CX 221 A,B – Total Domestic TiO_2 capacity 1970–1971
Appendix B: CX 222 – Total Domestic Shipment of TiO_2, Excluding Exports
Appendix C: CX 223 A,B – Total Domestic Shipment of TiO_2, Including Imports, Excluding Exports 1970–1977
Appendix D: CX 224 – Total Domestic TiO_2 Production Via the Sulfate Process/1970–1977
Appendix E: CX 225 – Total Domestic TiO_2 Production Via the Chloride Process 1970–1977
Appendix F: CX 133L – Mill Costs of TiO_2 producers at Capacity
Appendix G: CX 133I – Industry Sales and Capacity.
Appendix H: CXCPF p. 41– Comparison of DuPont Market Share Projections February/July 1972 [A–50]

CHART 2: Total Domestic TiO_2 Pigments Capacity/1970-1977 (In Tons). (Source: Chemical Economics Handbook, Stanford Research Institute, June 1978) 1/

TOTAL DOMESTIC TiO_2 PIGMENTS CAPACITY
1970-1977 (In Tons)

	1970		1971		1972		1973		1974		1975		1976		1977	
	Tons	Share	Tons	Share	Tons	Share	Tons	Share	Tons	Share	Tons	Share	Tons	Share	Tons	Share
DuPont 2/	252,000	30.0%	277,000	33.0%	327,000	37.5%	368,000	39.7%	313,000	35.2%	368,000	38.9%	425,000	43.5%	425,000	46.0%
NL Industries 3/	268,000	32.0%	269,000	31.9%	232,000	26.6%	221,000	23.9%	232,000	26.1%	232,000	24.4%	204,000	20.9%	140,000	15.1%
American Cyanamid	90,000	10.7%	82,000	9.8%	92,000	10.6%	112,000	12.1%	112,000	12.6%	112,000	11.8%	112,000	11.5%	112,000	12.1%
SCM 4/	78,000	9.3%	78,000	9.3%	78,000	9.0%	78,000	8.4%	82,000	9.2%	112,000	11.8%	113,000	11.6%	125,000	13.5%
Gulf & Western	70,000	8.3%	70,000	8.3%	70,000	8.0%	70,000	7.6%	73,000	8.2%	73,000	7.7%	73,000	7.5%	73,000	7.9%
Kerr-McGee	37,000	4.4%	39,000	4.6%	45,000	5.2%	50,000	5.4%	50,000	5.6%	50,000	5.3%	50,000	5.1%	50,000	5.4%
Sherwin-Williams 4/	27,000	3.2%	27,000	3.2%	27,000	3.1%	27,000	2.9%	27,000	3.0%	-	-	-	-	-	-
PPG 5/	18,000	2.1%	-	-	-	-	-	-	-	-	-	-	-	-	-	-
TOTALS	840,000	100%	841,000	100%	871,000	100%	926,000	100%	889,000	100%	947,000	100%	977,000	100%	925,000	100%

1/ Because the capacity figures are year-end rather than an integrated average for the year, the calculated operating rate is not precise and is sometimes understated. It has generally been accepted that the effective operating capacity of most plants, taking into account normal downtime, is about 90% of nameplate. This table lists an estimated annual nameplate capacity history for the years 1970 through 1977. (See 788.5002 B.)

2/ 55,000 tons of sulfate productive capacity located at Edge Moor, Delaware closed in 1974 and replaced by 55,000 tons of chloride productive capacity located at Edge Moor. This chloride conversion is recorded in capacity figure of 1975.

3/ NL shut down its St. Louis, Missouri 100,000 TPY sulfate plant in late 1977 or early 1978 for environmental reasons.

4/ CX 1008D; CX 1010C; Chemical Economics Handbook, February 1975, p. 577.4202 P-Q. Sherwin-Williams' 27,000 TPY TiO_2 pigments plant located in Ashtabula, Ohio is allocated to Sherwin-Williams' capacity for 1974 even though the plant was acquired by SCM on October 12, 1974.

5/ Answer to Specification 2 of August 20, 1975 subpoena duces tecum.

CHART 3: TOTAL DOMESTIC SHIPMENTS OF TiO_2 PIGMENTS BY U.S. PRODUCERS (EXCLUDING EXPORTS)

1970 - 1977

(Million Dollars and Nearest One Percent)

	1970	1971	1972	1973	1974	1975	1976	1977
Du Pont	96	94	109	141	195	190	257	290
	30%	30%	30%	33%	38%	41%	41%	42%
NL	107	98	101	112	103	90	108	115
	33%	32%	28%	26%	20%	20%	17%	17%
American Cyanamid	23	29	42	43	53	48	68	74
	7%	9%	12%	10%	10%	10%	11%	11%
SCM	26	26	29	36	44	50	74	80
	8%	8%	8%	8%	9%	11%	12%	12%
Gulf + Western	13	11	30	35	44	32	44	54
	4%	3%	8%	8%	9%	7%	7%	8%
Kerr-McGee	15	12	22	25	29	33	42	41
	5%	4%	6%	6%	6%	7%	7%	6%
Sherwin-Williams	8	12	14	17	18			
	2%	4%	4%	4%	4%			
Cabot	12	10						
	4%	3%						
PPG	4	4						
	1%	1%						
Subtotal	304	297	347	408	485	443	592	653
	94%	95%	94%	95%	95%	96%	95%	95%
Other Imports	21	15	22	20	28	19	29	39
	6%	5%	6%	5%	5%	4%	5%	5%
TOTAL	325	312	369	428	513	462	621	692

CHART 4: TOTAL DOMESTIC SHIPMENTS OF TiO_2 PIGMENTS (TRILLIONS; UNITS, EXCLUDING EXPORTS) 1970-1977 (IN 1000 TONS)

(SHIPMENTS ROUNDED TO NEAREST 1000, MARKET SHARE ROUNDED TO NEAREST WHOLE NUMBER)

	1970		1971		1972		1973		1974		1975		1976		1977	
	Tons	Share	Tons	Share	Tons	Share	Tons	Share	Tons	Share	Tons	Share	Tons	Share	Tons	Share
DuPont 1/	199	29%	214	30%	239	30%	286	34%	287	38%	239	40%	296	40%	320	41%
NL Industries 2/	203	30%	202	29%	201	25%	208	25%	149	20%	115	19%	126	17%	128	16%
AM CY 3/	51	8%	70	10%	90	11%	87	10%	80	11%	63	10%	78	11%	80	10%
SCM 3/	56	8%	62	9%	72	9%	71	8%	67	9%	76	13%	98	13%	99	13%
Kerr-McGee 3/	31	5%	36	5%	45	6%	48	6%	44	6%	44	7%	51	7%	48	6%
Gulf & Western 4/	30	4%	25	4%	61	8%	71	8%	63	8%	41	7%	51	7%	59	8%
Cabot 5/	24	4%	23	3%	-0-	-	-0-	-	-0-	-	-0-	-	-0-	-	-0-	-
Sherwin-Williams 7/	15	2%	25	4%	29	4%	30	4%	26	3%	-0-	-	-0-	-	-0-	-
PPG 9/	9	1%	9	1%	-0-	-	-0-	-	-0-	-	-0-	-	-0-	-	-0-	-
SUBTOTAL	618		666		737		801		716		578		700		734	
All Other Imports 10/	58	9%	41	6%	58	7%	45	5%	35	5%	25	4%	37	5%	49	6%
TOTAL	676	100%	707	100%	795	100%	846	100%	751	100%	603	100%	737	100%	783	100%

1/ CX 1(D; 18D; 19D; 42D; 66D; 127D; 151D; 189D; CX 190W; Letter dated 12/4/78 to William J. Murphy, Attorney, Bureau of Competition, from Mark Levy, Counsel for DuPont, (DuPont No. 57342) (CX 217).

2/ CX 901A; 902A; 903A; 904A; 905A; 906A; 907A; 908A; Letter dated 11/17/78 to Robert Doyle, Attorney, Bureau of Competition, from Arthur J. Mannion, Jr., Senior Staff Counsel, NL Industries, Inc.

3/ CX 6(GD; CX 6070; CX 6(0D; CX 6090; CX 6100; CX 611B; CX 6128; CX 6130; CX 6140; CX 6150; CX 6160; CX 6170; CX 6180; CX 6190; CX 6200; CX 621B; CX 6228; CX 6230; CX 6240.

4/ CX 502B; 503B; 504B; 505B; 506B; 510B; 553C; 503B; 510B.

5/ CX 5(1D; 8(4D; 804N; 807N; 808N; 809N; 810C; 811D.

6/ CX 700D; 701B; 702N; 703N; 704D; 705D; 706D; 707B; 708D; 709D; 710D; 711B; 712D; 713D.

7/ CX 1003A; CX 1004D; CX 1005A; CX 1006D; CX 1007D.

8/ 1970, 1971 Annual Reports to Bureau of Mines.

9/ 1975, 1971 Annual Reports to Bureau of Mines.

10/ CX 2V; CX 3V; CX 4C; CX 42C; CX 66C; CX 124C; CX 506D; CX 610D; CX 621B; CX 901A; CX 902A; CX 903A; CX 904A; CX 907A; CX 908A; U.S. Department of Commerce, Bureau of the Census, U.S. Foreign Trade - Imports TSUSA Commodity by Country, FT 246 (data for 1970-1977). (These figures include imports of TiO_2 pigments by: firms other than the domestic producers.) See also letter dated 11/17/78 to Robert Doyle, Attorney, Bureau of Competition, from Arthur J. Mannion, Jr., Senior Staff Counsel, NL Industries, Inc.

Chart 5: Total Domestic TiO_2 Pigments Production Via The Sulfate Process 1970-1977 (In Tons).

TOTAL DOMESTIC TiO_2 PIGMENTS PRODUCTION VIA THE SULFATE PROCESS
1970-1977 (In Tons)

	1970		1971		1972		1973		1974		1975		1976		1977	
	Tons	Share	Tons	Share	Tons	Share	Tons	Share	Tons	Share	Tons	Share	Tons	Share	Tons	Share
DuPont 1/	42,800	11.7%	41,700	12.0%	53,700	15.1%	53,200	13.9%	45,100	12.7%	—	--	—	—	—	—
NL Industries 2/	192,888	53.0%	183,807	53.1%	162,702	45.7%	184,299	48.0%	166,257	47.0%	135,283	58.0%	98,366	45.1%	73,485	36.6%
American Cyanamid 3/	47,349	13.0%	48,348	13.9%	53,561	15.1%	51,657	13.5%	50,480	14.3%	31,172	13.4%	44,772	20.5%	43,190	21.5%
SCM 4/	48,370	13.3%	44,771	13.0%	45,613	12.8%	50,961	13.3%	48,814	13.8%	38,182	16.4%	40,148	18.4%	47,324	23.6%
Gulf & Western 5/	33,067	9.1%	27,395	8.0%	40,499	11.4%	43,492	11.3%	43,020	12.2%	28,626	12.3%	34,993	16.0%	36,830	18.3%
Kerr-McGee	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Sherwin-Williams	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
TOTAL	364,474	100%	346,021	100%	356,075	100%	383,609	100%	353,671	100%	233,263	100%	218,279	100%	200,829	100%

1/ CX 192A.
2/ CX 901A; 902A; 903A; 904A; 905A; 906A; 907A; 908A; NL documents 0614049 and 0615161 (complaint counsel's numbers) submitted in response to the June 13, 1978 subpoena duces tecum.
3/ CX 501C.
4/ CX 605D.
5/ CX 700B; 701B; 702B; 704B; 706B; 708B; 710A; 712A. (These documents contain the sulfate production data for Gulf & Western's sulfate plant at Gloucester, New Jersey.

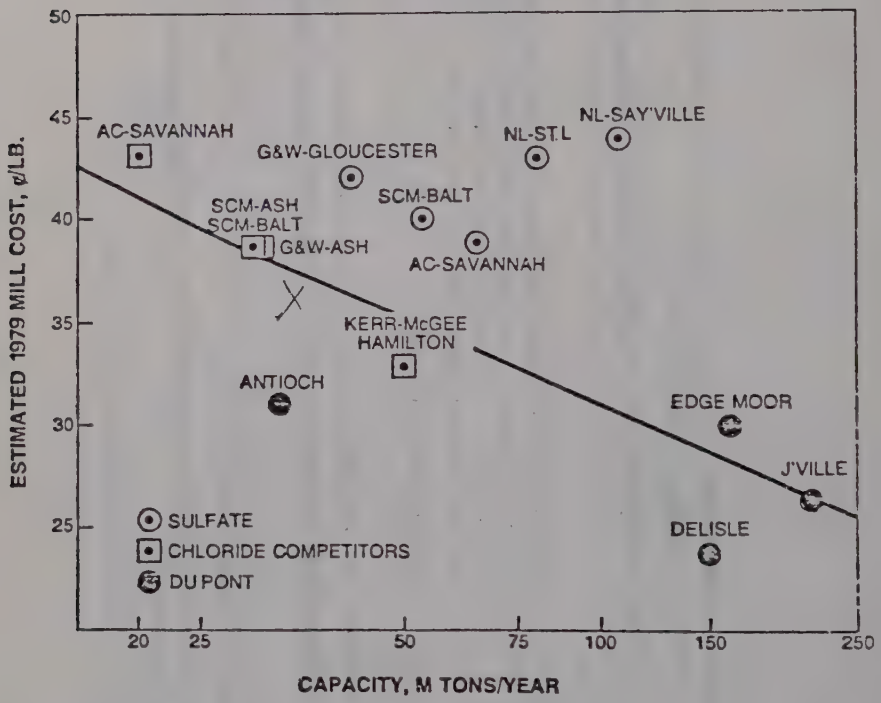
Exhibit 6. Total Domestic Production TiO_2 Pigments Via The Chloride Process (1970-1977 (In Tons).

TOTAL DOMESTIC PRODUCTION TiO_2 PIGMENTS VIA THE CHLORIDE PROCESS
1970-1977 (In Tons)

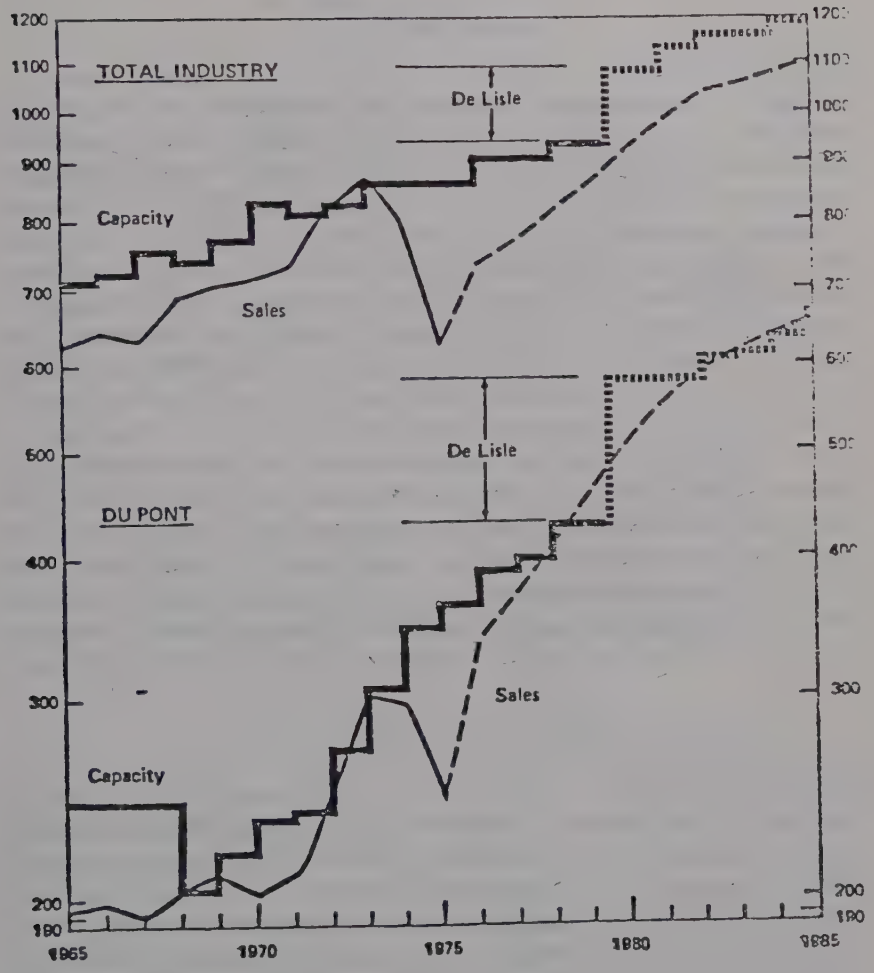
	1970		1971		1972		1973		1974		1975		1976		1977	
	Tons	Share	Tons	Share	Tons	Share	Tons	Share	Tons	Share	Tons	Share	Tons	Share	Tons	Share
Dupont 1/	161,000	57.4%	170,100	53.0%	200,900	58.4%	237,500	60.4%	272,400	63.1%	238,900	64.2%	310,100	64.5%	323,300	66.3%
NL Industries 2/	28,835	10.3%	20,805	6.5%	-	-	-	-	-	-	-	-	-	-	-	-
American Cyanamid 3/	6,407	2.3%	23,961	7.5%	33,215	9.5%	31,634	8.0%	34,739	8.0%	28,710	7.7%	37,744	7.9%	31,271	6.4%
SCM 4/	701	0.2%	12,784	4.0%	17,884	5.1%	21,113	5.4%	23,889	5.5%	40,346	10.8%	56,757	11.8%	60,455	12.4%
Gulf & Western 5/	-	-	-	-	25,492	7.3%	28,789	7.3%	28,083	6.5%	14,491	3.9%	23,870	5.0%	25,888	5.3%
Kerr-McGee 6/	33,472	12.0%	36,106	11.2%	41,952	12.1%	46,405	11.8%	48,120	11.1%	50,000	13.4%	52,034	10.8%	46,745	9.6%
Sherwin-Williams 7/	18,407	6.6%	26,363	8.2%	26,398	7.6%	28,134	7.1%	24,773	5.7%	-	-	-	-	-	-
Cabot 8/	21,416	7.6%	22,973	7.2%	-	-	-	-	-	-	-	-	-	-	-	-
PPG 9/	10,366	3.7%	8,048	2.5%	-	-	-	-	-	-	-	-	-	-	-	-
TOTAL	280,604	100%	321,140	100%	347,841	100%	393,575	100%	432,004	100%	372,447	100%	480,505	100%	487,659	100%

1/ CX190A.
2/ NL documents 0614047 and 0619161 (complaint counsel's numbers submitted in response to June 13, 1978 subpoena duces tecum. NL closed its chloride process TiO_2 pigments plant located at Sayreville at the end of 1972.
3/ CX 501C.
4/ CX 600D.
5/ CX 703D; 705B; 707D; 709B; 711D; 715B. (These documents contain chloride production data for Gulf & Western's chloride plant located at Ashtabula, Ohio.
6/ CX 804D; 805D; 806B; 807D; 808D; 809B; 810D; 811D.
7/ CX 1005D; 1006D; 1007B; 1008D; 1009B.
8/ 1970, 1971 Annual Reports to Bureau of Mines.
9/ 1970, 1971 Annual Reports to Bureau of Mines.

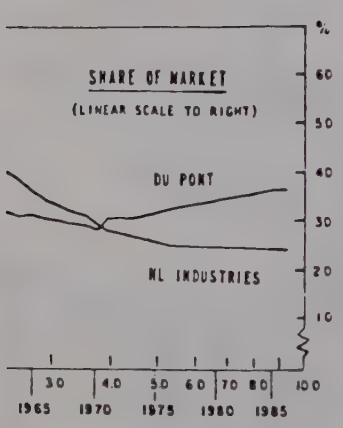
FIGURE 2: MILL COSTS OF TITANIUM DIOXIDE PRODUCERS



Titanium Dioxide Sales and Capacity
(Thousands of Tons)



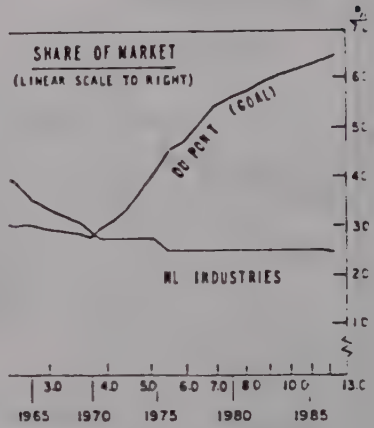
Comparison of Dupont Market Share
Projections: February/July 197.



source: CX 21 O

BEFORE "GROWTH STRATEGY"

February 10, 1972



source: CX 29 N

AFTER "GROWTH STRATEGY"

July 6, 1972

Opinion of the Commission

By Clanton, *Commissioner:*

Introduction

In challenging the legality of an expansion strategy adopted and carried out by respondent, E.I. DuPont de Nemours & Company ("DuPont"), in its titanium pigments business, this case addresses issues that are fundamental to antitrust policy. The complaint, issued April 5, 1978, charges DuPont in a two-part count with unfair methods of competition and unfair acts and practices by using its dominant position in an attempt to monopolize the production of titanium dioxide pigments ("TiO_2") in the United States, in violation of Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45. Administrative Law Judge Miles J. Brown (ALJ) dismissed the complaint and complaint counsel appeal.

The many events that compose the expansion strategy at issue span the years 1971 to 1978. As might be expected, these events are highly relevant to the issue of liability and, for that reason, must be set out in some detail, especially in view of the allegation that the expansion plan is unreasonable, and therefore unlawful, only [2]if assessed in its entirety. The actual occurrence of much of this conduct is largely uncontroverted, but the parties vigorously contest the legal consequences of these events.[1] (ID 5)

Respondent and the Market

DuPont is a Delaware corporation with its principal place of business at 1007 Market St., Wilmington, Delaware. In 1976, DuPont had sales exceeding $8.3 billion, assets exceeding $7 billion and net income exceeding $459 million. It is engaged in the manufacture and sale of diverse chemical and related products, among them pigments and dyes including titanium dioxide pigment. During the period in question, DuPont's TiO_2 production was the responsibility of its

[1] The following abbreviations will be used in this opinion.

ID	–	Initial Decision page number
IDF	–	Initial Decision Finding number
Tr.	–	Transcript page number
CX	–	Complaint Counsel's exhibit number
RX	–	Respondent's exhibit number
CAB	–	Complaint Counsel's appeal brief
RAB	–	Respondent's answering brief
CRB	–	Complaint Counsel's reply brief
Tr.OA	–	Transcript of Oral Argument page number

Pigments Department, and in 1976, DuPont's total domestic shipments of TiO_2 amounted to $257 million. (IDF 1–3, 6)

There is no dispute about the product and geographic markets at issue in this case. As there are no practical substitutes for the product, TiO_2 constitutes a distinct product market. The United States as a whole is the relevant geographic market for purposes of this case. (IDF 5)

TiO_2 is a white chemical pigment used in the manufacture of such products as paint and paper to make them whiter or opaque. In manufacturing TiO_2, there are two basic processes: the "sulfate" process and the "chloride" process. Essentially, the sulfate process involves the reaction of sulfuric acid with relatively low-grade feedstock (ilmenite ore or titanium slag), while the chloride processes entail the reaction of chlorine either with a high-grade titanium ore (rutile ore or synthetic rutile) or with lower grades of feedstock (principally ilmenite ore). During the relevant time frame, only DuPont used the latter chloride process. (ID 5) [3]

A brief background on these two processes is helpful. The sulfate process was the first developed and used by all producers, including DuPont. It is a "batch" process, not affording the economies of large scale inherent in the "continuous flow" operation of the chloride processes. In the post-World War II period, DuPont developed chloride technology and began applying it to the relatively abundant low-grade ilmenite ore for commercial purposes. By 1952 DuPont's first ilmenite chloride facility was fully operational at Edge Moor, Delaware, where it also had a sulfate facility. In 1958, DuPont opened a second ilmenite chloride TiO_2 plant at New Johnsonville, Tennessee. While DuPont was building chloride process TiO_2 plants in the 1950's, other producers continued to build only sulfate plants. (ID 5)

In the late 1950's, abundant rutile ore deposits were discovered, and from 1960 to 1970, all TiO_2 plants constructed, including DuPont's Antioch, California, plant, were designed to use rutile ore in a chloride process. Until the late 1960's, the overall costs of production of TiO_2 were essentially equal among the various combinations of processes and ores. Although DuPont alone possessed the technology (principally know-how) to make the chloride process commercially viable using ilmenite ore, the relative costs of rutile and ilmenite were such that no production process conferred a significant cost advantage. (ID 5–6) So long as rutile ore was plentiful, a high-grade rutile chloride plant yielded a better return on investment than a comparable low-grade ilmenite process plant, due to the relative costs of ores, chlorine, waste disposal and initial

investments (which were lower for the high-grade ore plant). (IDF 17)

DuPont's development of the ilmenite chloride process through the transition from the laboratory stage to commercial production unquestionably proved to be a difficult and notable technological achievement. Although DuPont developed this process in small operating units, the small-scale production technology could not be readily transferred to larger-scale commercial production. Thus, new techniques had to be devised to adapt the chloride process to increasing scales of operation. (IDF 16)

Around 1970, a world-wide shortage of rutile sent its price soaring. Also at about that time, federal environmental regulations imposed costly pollution abatement requirements upon sulfate TiO_2 producers, threatening to close down some of the sulfate capacity. As a result, DuPont's ilmenite chloride process left it holding a substantial cost advantage (unit cost of about 16¢/lb) over its competitors (about 21¢/lb). (ID 6, CX 28E) [4]

It was DuPont's decision in 1972 to exploit this advantage and to increase its market share that gave rise to the complaint in this case. From 1972 to 1977, DuPont expanded its capacity and increased its market share from approximately 30% to 42%, and it presently forecasts that it will achieve a 55% share by 1985. Since 1970, no TiO2 competitor has added new production capacity. (ID 6)

The Allegations

The complaint charges DuPont with an attempt to monopolize the TiO_2 market by the adoption and implementation of a strategy or plan to expand its domestic TiO_2 production capacity to capture substantially all of the growth in domestic demand for TiO_2 through the mid-1980's. Crucial to the plan was DuPont's undisputed cost advantage over its rivals in production of TiO_2, which stemmed both from economies of scale and from DuPont's unique technological ability to use lower-grade (and lower cost) ilmenite ore. In this respect, complaint counsel contend that DuPont's cost advantage was "fortuitous," conferred upon it accidentally by the increases in the price of rutile and the costs of waste disposal in the sulfate process.

As alleged, DuPont's growth strategy consists of three interrelated elements: a) expansion of capacity by construction of a large-scale plant; b) exploitation of its cost advantage by pricing its products high enough to finance its own expanded capacity, yet low enough to discourage rivals from expanding; and c) refusal to license its cost-

saving ilmenite chloride technology with which rivals could learn to take advantage of the economies of scale inherent in the low-grade ore technology. In addition, the allegedly strategic behavior of DuPont consisted of premature expansion of its TiO_2 capacity and exaggerated announcements of its expansion intentions, all for the primary purpose of preempting competitors' expansion plans.

Complaint counsel contend that this conduct amounted to exclusionary and anticompetitive behavior insulating DuPont's cost advantage from competitive erosion since the ilmenite chloride technology actually changes as the scale of operation increases and, without large-scale operations, no competitor will be able to reduce or eliminate DuPont's cost advantage through "learning-by-doing" ilmenite chloride technology. The inevitable result of this strategy, according to complaint counsel, will be to give DuPont the power to raise prices at will, restrict output and prevent competition. (ID 43) Indeed, complaint counsel argue that DuPont's expansion plan "made no sense unless it results in a monopoly." Tr. OA 17. [5]

DuPont admits that it sought to capitalize on its cost advantage in order to capture or serve the major portion of the growth in demand for TiO_2 well into the 1980's. (RAB 12) Even so, it denies that the cost advantage was "fortuitous," claiming instead that it was due to its costly innovations in low-grade ilmenite chloride technology in earlier years. It further denies that its capacity expansion had any purpose other than to satisfy the expected increase in demand for TiO_2. DuPont also denies that it engaged in an unlawful strategic pricing strategy, contending that its pricing during the period was attributable to market forces beyond its control. (RAB 27) Indeed, DuPont asserts that complaint counsel failed to prove that its prices were not profit-maximizing under the prevailing economic conditions. *Id.*

Furthermore, DuPont claims that it was under no duty to license its ilmenite chloride technology to any competitor, and contends that its competitors, all large corporations engaged in TiO_2 manufacture, are not prevented from developing their own low-grade ore technology or constructing large scale plants if they choose to make such investments. (RAB 28) Finally, DuPont points to its failure to achieve the anticipated growth in its market share and denies that it could attain monopoly power in the TiO_2 market. (RAB 43 *et seq.*)

We proceed now to a fuller exposition of the events giving rise to this case.

The Strategy

Prior to its switch to a more aggressive growth strategy, DuPont had some limited TiO_2 expansion plans underway. Specifically, respondent sought to expand its sales from 218 thousand tons per year ("MT") in 1971 to 301 MT in 1976, including an increase in the chloride capacity at New Johnsonville from 141 MT to 196 MT, which would make it the world's largest TiO_2 plant.[2] At that time, DuPont's pricing policy was to maintain prices, except to cover inflation, until 1986 in conjunction with its conversions and expansions. (CX 22A) Its share of the TiO_2 market stood at 30%. (CX 21) [6]

In early 1972, however, DuPont noted that significant changes had occurred or were occurring in the TiO_2 market, including the fact that National Lead ("NL") and PPG were shutting down rutile chloride plants due to price erosion during the recession, that NL had ceased making "extended pigment," thus taking even more product off the market, and that the industry had little reserve capacity, although demand was recovering from the recession. (CX 21) Later that year, DuPont became further aware of its advantageous position when its Development Department formed a Task Force to improve the performance of the Pigments Department. The Task Force focused on the coming decline of sulfate capacity, DuPont's expanded scale and its 5¢/pound cost advantage over its competitors, the rutile supply problems of competitors, the waste disposal differences between sulfate and chloride, and the fact that competitors could technically convert to ilmenite but that at their scales of production it was too expensive and risky to do so.[3] (CX 23) The Task Force reported those developments to the Executive Committee and predicted that DuPont could capture all of the anticipated increase in demand (from 713 MT in 1971 to 1000–1100 MT in 1980) and attain a market share of 56% by 1980 and perhaps 65% by 1985.

In light of these apparent long-run opportunities, DuPont decided in 1972 to launch the more aggressive expansion strategy. It attributes its decision specifically to a) recovery of the economy from the recession, b) a surcharge on imports, c) the impending and actual

[2] As background, it should be noted that in 1971 DuPont had both sulfate and chloride process plants. But because of the increasing costs of the sulfate process, in 1971 the Pigments Department recommended exclusive reliance on the chloride process and conversion of sulfate capacity at Edge Moor to ilmenite chloride production. (CX 15)

[3] DuPont believed that the basic ilmenite chloride patent technology had been disclosed in scientific literature, but its competitors continued to use the rutile chloride process. In DuPont's view, they were reluctant to shift to ilmenite technology because they shied away from ilmenite waste disposal problems and they lacked sufficiently large-scale plants to justify the expense of conversion. (CX 16A–F)

decrease in sulfate and rutile chloride capacity throughout the industry and d) DuPont's cost advantage in using ilmenite together with the scale economies achieved through expansions at Edge Moor and New Johnsonville. (RAB 11) Complaint counsel contend that no exogenous market change led to the reassessment, but that DuPont simply sought to prevent competitive expansion and attain monopoly power. Although the documentary record reveals little about the reasons leading DuPont to rethink its strategy, complaint counsel are correct in asserting that the principal market changes justifying the growth strategy mostly occurred prior to DuPont's adoption of its earlier, more moderate expansion program. [7]

The initial terms of the new expansion plan called for upgraded capacities of 167 MT for Edge Moor (from 110) and 228 for New Johnsonville (instead of 196), and for a third ilmenite chloride plant at "Site X," originally envisioned as two lines commencing at staggered times, with a capacity range between 110 and 380 MT. (CX 26F, H, CX 38L, CX 50B, H)

While such capacities were large for the industry, from the outset, DuPont's expansion plans appeared to involve plants of optimally efficient scale. DuPont's estimate of the increase in demand between 1972 and 1980 was 330 MT, which DuPont characterized as equivalent to "three fully developed JV-type [New Johnsonville] lines" (110 MT each). (CX 34I, CX 26D–E) Later planning documents retained 110 MT as a benchmark capacity in the proposal for a 110 MT line by 1980 at Site X and an "innovative" second line of 220 MT there in the indefinite future. (CX 38L) Throughout the planning period 1972–73, DuPont's technological applications improved and the plan was revised to expand New Johnsonville to 252 MT (two lines). With the increase in the optimal scale of the JV-type line to 126 MT, the planned capacity of the future single line at Site X increased to 130 MT.[4] (CX 26H, CX 54A) There is no evidence that DuPont planned to build excess capacity or that its plans to fulfill the foreseen demand with new and expanded plants were inconsistent with scale economies.

As mentioned above, the Task Force expected the remainder of the industry to suffer a net loss of capacity. DuPont's estimate of its competitors' 1972 capacity was 480–505 MT, which included 160 MT of sulfate capacity that was expected to be shut down due to environmental difficulties. (CX 26M) DuPont anticipated a limited expansion of competitors' chloride capacity before 1980, which would replace some of the lost sulfate production. Specifically, DuPont

[4] The capacities of 167 for EM and 252 for JV were the "desired practical limits" of those plants; expansions to those limits were actually begun in May 1974. (CX 54C)

expected Kerr-McGee to gain a net increase of 50 MT (chloride), while expansion by others was less certain.[5] In no event was competitive chloride expansion expected to exceed 110 MT by 1980, compared to the projected loss of 160 MT of sulfate capacity. The 1972 appropriation request for the expansion of New Johnsonville noted that PPG and NL were abandoning chloride plants due to unfavorable economics, that Cabot had transferred its chloride plant to Gulf & Western, that remaining industry capacity was oversold and that industry expansion was necessary to meet forecast demand. (CX 29H–I) [8]

Complaint counsel accuse DuPont of perpetuating these discouraging conditions for competitors by pricing in a manner that made it unattractive for other firms to invest in new capacity. While pricing to generate funds for expansion was an integral part of the 1972 strategy, discouragement of competitive expansion did not appear as an express element of the strategy until 1975, at least in presentations to the Executive Committee.[6] As for DuPont's individual pricing decisions throughout the period 1972–1977, there is some additional evidence to suggest that those decisions took account of the effect upon competitive expansion. At the same time, the record indicates that respondent's pricing strategy underwent periodic adjustment due to variations in market forces, including cost inflation and amended demand forecasts.

Complaint counsel cite several events that allegedly reveal DuPont's pricing policy to prevent competitors from earning sufficient funds to expand. In one such instance, Kerr-McGee increased its TiO_2 price by 3¢ in June 1972, an action that DuPont personnel understood to be related to the desire of certain competitors to expand. Complaint counsel contend that it was DuPont's unilateral refusal to follow the price increase, not market forces, that prevented the price hike. However, DuPont proved unable to prevent an increase—because of a lack of excess capacity, DuPont could not force a roll-back of prices to its level, and two-tier pricing resulted. (RAB 25) Although the documents show that the expansion-inducing effects of the increase played a role, other market-related reasons influencing DuPont's decision were that: a) DuPont's larger customers had price protection (a firm price) until the end of the year, b) there was uncertainty about federal price controls, c) an increase would stimulate imports, d) an increase during a shortage looked

[5] Expansions of 25 MT by American Cyanamid and 35 MT by SCM were assigned low (10%) probabilities, (CX 213B) and apparently expansions by other firms were even less likely.

[6] Express elements of the 1972 strategy were to a) price to generate funds for expansion, b) decide the configuration of production facilities (a third site was needed), c) increase the mineral supply and d) decide on a waste disposal method. (CX 27F)

like gouging, and e) DuPont's price was already higher than some competitors'. (CX 28)

Subsequently, DuPont increased its prices on four separate occasions in 1974. (CX 3, #196–200) The record fails to show whether DuPont led all of these increases, although in its brief respondent states that it led the last one, which had to be partially rescinded. (RAB 27) In January 1975, after these four increases, DuPont, citing market softness, again refused to support a competitor's 5¢ increase, and all competitors rolled back their prices. (CX 3, #201–09) However, six months later, DuPont led another, lesser price increase of 3.5¢, which competitors followed. (CX 3, #210–14) This time DuPont thought the increase was a compromise [9]level for restoring earnings in the face of rapidly rising costs without shrinking demand. (RX 2B) Due to excess capacity and discounting, this latter increase was only partially successful. Nevertheless, complaint counsel cite this sequence of events as evidence of DuPont's power to control prices and its policy of restricting competitors' revenues.

Two other pricing patterns were discussed. In both 1976 and 1977, competitors led increases but, when DuPont raised its prices by a lesser amount, the competitors rescinded to the smaller increase. In 1976, DuPont cited the effects of the price hike on its customers and on imports, while in 1977 DuPont believed that the smaller increase would help it keep its market share, would minimize substitution of "extenders" for TiO_2, would be more palatable to customers, and would approximate recent cost increases. (CX 161)

While an interest in discouraging expansions by competitors could be inferred from the totality of the pricing policies and conduct, substantial alternative reasons attributable to external market forces were also evident, and neither of the explanations is necessarily inconsistent with what occurred in each instance. In reviewing the strategy, the 1975 Task Force inferred that, from the outset, the pricing policy had the dual purpose of providing cash for expansion and limiting competitors' ability to expand. On the other hand, as we discuss further below, it appears that independent market factors may have led DuPont and competitors to price at levels below the expansion-inducing (or limit) price that would have prevailed under more favorable market conditions.

Complaint counsel also contend that DuPont strategically announced its intentions to build new capacity and actually began such expansions prematurely, for the primary purpose of preempting and discouraging competitors' expansion opportunities. (CAB 15) For example, in July 1974, an appropriation request was made for the "partial design, a construction cost estimate, and cancellation

charges on long-term delivery equipment" for a 130 MT chloride plant at De Lisle, Mississippi. (CX 3, #114) DuPont also described this action as a decision "to authorize funds for a preliminary engineering study into a third TiO_2 chloride" plant. (CX 3, #126) By comparison, the press release of July 16 declared that DuPont planned to construct a plant on a site then under option and that it had authorized expenditure of $8 million for a "detailed design and order of long delivery equipment." (CX 159F) Complaint counsel argue that DuPont's announcement of this appropriation, among others, was both premature and exaggerated. The ALJ found that such announcements were necessary to inform customers and the De Lisle community of DuPont's plans. (ID 41) While a "detailed design" suggests more of a commitment than a "preliminary engineering study," this disparity in the announced scope of DuPont's intentions does not seem sufficient to mislead [10]sophisticated corporate managers, especially since the amount of expenditure was disclosed. In addition, DuPont's customers were anxious to know whether DuPont would supply their anticipated increased needs. Furthermore, DuPont had encountered environmental resistance in its first choice of sites, and because of the time required to license such a facility, it was reasonable to give early notice to the community, to licensing authorities and to customers. For these reasons, it appears that the scope and timing of DuPont's announcements of its intentions regarding De Lisle were related to legitimate business considerations.

Complaint counsel also allege that DuPont's decision on the timing of De Lisle's start-up amounted to another of the strategic decisions aimed at preventing competitive expansion, and that DuPont eventually decided to bring De Lisle on-stream "early." (CAB 37) Yet complaint counsel acknowledge that an accelerated start-up would not result in oversupply. *Id.* From the outset, the start-up of De Lisle was planned to coincide with the increase in demand that the economic recovery of the late 70's was expected to bring. The Pigments Department emphasized the advantages of proper timing in urging the Executive Committee not to delay the start-up:

> Although this action (reaming out existing facilities and delaying the start-up until 1981) reduces cash needs during 1975–1978, it has serious long run implications. . . . At a later date, it would be impossible to regain this momentum because the lack of major activity by DuPont in the interim would prompt competition to implement their own expansion plans. Therefore, sell-out of a De Lisle-type plant would require about ten years rather than the desired 3–4 years . . . [since] DuPont would be facing the prospect of competing on a "me-too" basis. (CX 71F)

This document and other Task Force memoranda indicate that the

decisions regarding the commencement of production at De Lisle were consistent with both a desire to respond to market opportunities and a desire to expand before competitors expanded.

We also note that there are no allegations that the size of the De Lisle proposal was excessive or inconsistent with optimal scale economies. When the De Lisle plans were first assembled, the equipment specifications from New Johnsonville were used, yielding a projected capacity of 130 MT. By 1975, DuPont had recalculated the capacities of the equipment for use at De Lisle, taking improvements into account, and up-graded the projected efficient capacity to 150 MT. (CX 113J) The plans for a second line at De Lisle were later postponed indefinitely. [11]

In 1975, a general economic recession led the DuPont Executive Committee to reevaluate about ten capital projects, and a slump in TiO_2 sales in particular led it to review the De Lisle construction plans. The Pigments Department found its De Lisle project competing for funds with several other corporate projects. To make its case for the De Lisle project, the Task Force devised two alternative ten-year TiO_2 business strategies—one an aggressive "growth" plan calling for completion of De Lisle and aiming toward 60% of the market, the other a "maintain" strategy aimed at a 43% share with no new plant until 1985. (CX 91) To convince the Executive Committee not to abandon or delay De Lisle, the Task Force focused on the long-run profitability of the TiO_2 business with the added capacity and a larger market share. Much attention in the parties' briefs is devoted to the extent to which the Executive Committee was exposed to and adopted the plans and recommendations of the reconstituted TiO_2 Task Force.

In attempting to estimate the effect of TiO_2 prices on DuPont's ability to sell out De Lisle within three or four years of the plant's opening, the Task Force performed the following calculations: price that would trigger competitive expansion, price that would trigger imports, price at which TiO_2 substitutes occur, price that will sink any firm. (CX 85B) The express pricing goal under the "growth" strategy was to price as high as possible to generate expansion funds without a major competitive expansion or foreign entry. Under the "maintain" strategy, the pricing policy would be "to balance profit with limited competitive expansion and foreign entry."[7] (CX 113P)

[7] The return on investment in TiO_2 was significantly higher for DuPont than for its competitors. DuPont documents describe the TiO_2 business as a profitable one for itself but a marginal one for competitors. (CX 182E) While DuPont's operative return on investment was 29% in 1972, its estimates of competitors' returns were as follows: Kerr-McGee and American Cyanamid, 8%; SCM and Cabot, 3%; NL Industries, 12%. (CX 26M) The projected return on the De Lisle project was also higher than that for DuPont's overall TiO_2 operations. The projected *net* return on the De Lisle project by the third year of operation (1981) was 17% while the projected net return on DuPont's entire TiO_2 business for the third year was 15%. (CX 133N)

The documents indicate the Task Force's belief that if De Lisle were delayed one year, competitive expansion was unlikely (CX 101), but that if De Lisle were abandoned, Kerr-McGee, SCM and American Cyanamid might expand. (CX 108) However, in its presentation to the Executive Committee, the Task Force predicted that any delay of De Lisle would stimulate others to expand. In turn, it was argued, such expansion would preclude DuPont from attaining full capacity within the four-year period thought necessary to make De Lisle economically viable. (CX 116I)

The Task Force also prepared several comparative long-range projections of the price and profit expectations under the two proposed strategies, projections that are referred to in the briefs as the "welfare analysis." These projections showed that, while TiO_2 prices would be lower in 1980 under the growth plan than under the "maintain" strategy, after 1984 the prices, and thus the [12]total profitability out to 1992, would be higher under the expansion plan. The welfare analysis itself contains no explanation of the different price assumptions used, but other documents referred generally to the value of a larger market share. (CX 116J)

Complaint counsel argue that the welfare analysis shows that DuPont knew that it would recoup any sacrifice of short-run profit by higher long-run prices which, they contend, would result from DuPont's higher market share and future monopoly power over price. Complaint counsel also contend that, because the Executive Committee chose to build De Lisle despite the fact that the third-year rate of return was lower than that in the "maintain" strategy projection, the upper management of DuPont must have looked beyond its normal three-year investment evaluation period and intended a predatory, short-term sacrifice of profits. By complaint counsel's calculations, DuPont will reap $387 million more between 1975 and 1992 under the growth strategy than it would under the "maintain" plan.

DuPont responds that the two tables of projected market variables called the "welfare analysis" do not mean what complaint counsel claim they do. According to the testimony of Mr. Clark, the Pigments Department's manager for research and development, the planning period for the De Lisle project ran only to 1985. The projected price in that year would be higher for the "growth" strategy than for the "maintain" strategy, in the judgment of the Task Force, because of the following scenario: If De Lisle were delayed, prices would first rise, reflecting a shortage. However, competitors would eventually bring on new capacity in an uncoordinated manner, resulting in overcapacity. Prices would then fall or at least stabilize despite

rising costs for a period of years. By 1985, the overcapacity would cause prices to drop 2¢/pound below the projected level under the growth strategy, due to excess capacity. Mr. Clark's testimony is that the projection of prices beyond 1985 was a purely mechanical application of factors to produce DuPont's uniform investment evaluation benchmark, the investor's method rate of return, for the full period of depreciation (13 years). (Tr. 1286–91, 1455–59) Mr. Clark explained that while the 2¢ differential in 1985 resulted from Task Force judgment about the scenario, the computer simply escalated the numbers out to 1992 in the same relationship as they stood in 1985. Mr. Clark also vigorously denied that anticipation of larger market share played any role in the projections. (Tr. 1299, 1323, 1385, 1468)

From the documentary evidence, it seems reasonable to infer that the Task Force projections were used in the presentation to the Executive Committee and that the Committee was aware of the conceptual, if not the actual, projected price differential between the two strategies, despite testimony that the differential was not a factor in the De Lisle decision.[8] While the 1992 projections do not appear to [13]reveal any specific assessment of the factors that would affect prices beyond 1985, the projections nevertheless indicate that DuPont would gain some pricing advantage if it built De Lisle and thereby prevented a period of overcapacity. But, weighed in its context, the "welfare analysis" reveals little about the extent to which DuPont would exercise its market power.

In addition to the projected price differential, several other factors were discussed by the Task Force in preparation for the presentation to the Executive Committee. One topic presented to the Committee was the retention of DuPont's TiO_2 customer base, while a topic apparently dropped from the written presentation was the preemptive impact upon competitors of DuPont's announcements of its expansion plans.

As for customer relations, DuPont believed that

> [a] portion of our market share growth over the past years stems from bringing on additional capacity at times when it was needed. Another portion resulted from the expectation on the part of customers that we would continue to expand to meet their growth needs. (CX 118A)

By 1975, De Lisle had already been announced and customer expectations established. Having created such expectations, DuPont

[8] Mr. Shapiro, DuPont's chairman, testified that while the short-run profitability of reaming out and expanding New Johnsonville exceeded the short-run profitability of building De Lisle, output from New Johnsonville would be inadequate to meet demand and DuPont would have to build another plant anyway, so it was more efficient and economical to proceed with De Lisle. (Tr. 799)

believed it had much to lose from reversing itself on De Lisle, especially its credibility as a supplier. To delay construction of De Lisle would be seen by customers as unwillingness to meet their future needs. To cancel would be worse, in the view of the Task Force, since competitors had been discouraged from expansion because of DuPont's "announced and well-publicized intentions." (CX 118A) DuPont would gain "an image of having forestalled competitive expansions on a false premise," and would thereafter be the least favored supplier. *Id.*

Such Task Force speculation about the preemptive nature of the announcements about De Lisle, as contrasted with the expansion itself, did not go beyond the Pigments Department. While the Task Force observed, in the draft of its presentation, that its well-publicized expansion plans had made competitors hesitant to expand, (CX 113F) there was nothing explicit about preemption of competitive expansions in the written discussion before the Executive Committee. (CX 116H) Nevertheless, it is reasonable to infer from the overall presentation that the Executive Committee clearly understood the full effects of such a large expansion. The Committee was told that the pricing structure had reportedly kept competitors from expanding; and it was also made aware of DuPont's scale advantages, customer expectations, the pricing structure, the political and environmental value of a new chloride production site and the differential in projected prices between the alternative strategies. After the presentation, the Executive Committee decided to continue [14]as planned with construction of the 150 MT De Lisle plant, to commence operation in 1979.[9]

This decision was believed to have

> signalled DuPont's intention to compete strongly for the increased needs of domestic industry into the early eighties. Customers, concerned about future shortages, and most competitors, aware of the many problems they face, appear to have accepted this. (CX 140H, CX 120U)

Even so, throughout the rest of the period, the Task Force remained concerned that, due to unanticipated slumps in demand, the strategy, which it continued to follow, would not yield sufficient revenues for De Lisle. In fact, however, between 1972 and 1977, DuPont's profit objectives were almost met, by its own account, by keeping its prices high, causing the Task Force to recommend a

[9] In examining the role of the Task Force, we have reviewed respondent's arguments that it should not be held accountable for the brainstorming of lower-level management. It is clear, however, that the Task Force constituted much more than a "think tank" operation. It was specifically set up to develop a long-range plan for the Pigments Department and its basic recommendations were consistently followed by the Executive Committee. Moreover, the Task Force's periodic reassessment of the 1972 strategy, and its revisions, leave little doubt as to senior management's endorsement of the basic elements of the growth strategy. (CX 178, 180, 182).

program of lower prices to encourage consumption of TiO_2. (CX 182F)

As originally conceived, the growth strategy did not call for DuPont to take market share or existing sales away from competitors; rather, the plan was to capture the forecast growth in demand. As it turned out, over the course of the strategy, DuPont did take some market share from its competitors. Despite DuPont's early forecasts and expectations, between 1972 and 1977 there was no net increase in total demand for TiO_2 and competitors' sulfate plants did not close. While it fell well short of its earlier market share goals, DuPont nevertheless increased its sales over the period by 80 MT, at the expense of competitors.

By late 1977, no competitive expansion was foreseen. The final injection of funds for the start-up of De Lisle was being fine-tuned to coincide with the anticipated economic recovery at which the output was aimed. (CX 196H, CX 159B) [15]

Summary of Facts

We have here a remarkably clear blueprint of DuPont's plan to capture all or most of the increased demand for TiO_2 after 1972. Although DuPont has fallen somewhat short of its 1972 market share goals—51.8% planned vs. 43% actual for 1978—it nevertheless has continued to follow the early strategy. The principal setbacks resulted from a slowdown in demand growth and the continued operation of sulfate plants that DuPont thought would be closed due to pollution problems. These circumstances also forced DuPont to cancel (or at least indefinitely postpone) a second line at De Lisle. As to much of the evidence there is little dispute about the precise events that occurred or the sequence of these events. Where the parties diverge sharply is over the inferences to be drawn from DuPont's conduct and, more specifically, over the justifications offered in defense of the expansion and pricing decisions.

As for the expansion program, the record is quite clear that DuPont's plans left little room for competitors, with the possible exception of Kerr-McGee, to expand by 1980. At the same time, it is also clear that DuPont did not seek to drive competitors out of the market, although the effect of capturing all growth would inevitably be to reduce the market share of other competitors and, arguably, the value of that share. There is no evidence to indicate that DuPont's 1972 estimate of 1980 demand was unreasonable or exaggerated; indeed, a TiO_2 shortage existed in 1972 and the economic downturn of the mid-70's had not yet materialized. Had

DuPont expanded only its existing facilities to their "desired practical limits" (Edge Moor from 55 to 167, New Johnsonville from 141 to 252, and Antioch from 28 to 50), its addition of capacity would have fallen short of the projected 1980 increase in demand by about the amount of the projected capacity of De Lisle's first production line.[10]

Complaint counsel do not contend that DuPont overbuilt its capacity relative to anticipated demand; rather they argue that respondent met its growth objectives only by preempting competitive expansion through strategic announcement and start-up of the De Lisle plant as well as pricing to deter competitive growth. As examples of strategic timing, complaint counsel cite DuPont's 1974 announcement of its plan to build De Lisle, which occurred before funds were actually appropriated, and the 1975 recommendation to the Executive Committee urging that start-up of De Lisle not be delayed for two years (despite a market slump) because of competitive ramifications. [16]

On the other hand, as the law judge noted and complaint counsel recognize, there were legitimate business reasons for DuPont to provide as much notice as possible of its expansion plans. (ID 21, 41, CAB 36) DuPont had encountered strong environmentally related resistance in its attempts to locate what eventually became the De Lisle plant, and, in fact, the firm abandoned its first choice of sites in Georgia. Thus, early notice and clearance of a site was logical, and the period required for licensing such a facility appeared substantial. In addition, as the record indicates, there were customer-related reasons for providing adequate advance notice about capacity expansion and for not abandoning publicly announced expansion plans. In short, although DuPont systematically took account of the impact of its decisions on competitors, we cannot find that respondent timed the announcement and start-up of its De Lisle plant in a way that was unrelated to market growth, lead time and other legitimate business considerations.

It should also be emphasized that the significant scale economies achieved by DuPont in its ilmenite chloride process made it feasible for respondent to try and capture growth left unmet after expansion of its existing plants through construction of a large, efficient-size plant. Other than Kerr-McGee, with its contemplated 50 MT addition, DuPont appeared to be the firm most interested and capable of significant expansion before 1980. As market conditions

[10] That takes into account the 1972 projection that there would be a net loss of roughly 60 MT due to shutdown of sulfate plants. Because those shutdowns never occurred and demand growth slowed, the De Lisle plant was brought on stream later than originally anticipated.

changed throughout the period, DuPont revised both the size of the De Lisle plant and its start-up date to take account of the adjusted estimates of demand. While DuPont's original plans for its new plant site included a second line of 220 MT capacity, and while the press release announcing the first appropriation for De Lisle stated that the single-line plant was planned with expansion in mind, the second line at De Lisle was never formally announced to the industry and, indeed, quickly disappeared from the TiO_2 strategy.

As De Lisle neared completion, and after $142 million had been spent on the project, DuPont considered whether to delay or to accelerate its start-up. The final infusion of capital was to be timed so that completion coincided with the anticipated resurgence of demand. The costs already sunk as well as customer expectations were legitimate business reasons for DuPont to proceed with completion as urged by the Pigments Department in late 1977, even if it meant that the plant might lie dormant for a year.

On the pricing side, two interrelated issues are involved: DuPont's influence over price and the rationale for both the firm's individual pricing decisions and its overall pricing strategy. Central to complaint counsel's case is the allegation that DuPont deliberately sought to deter competitive expansion, and simultaneously effect its own expansion plans, by using its cost advantage to price at a level that would make it unattractive for competitors to enlarge their capacity. [17]In support of their position, complaint counsel rely on Task Force statements as well as four instances where DuPont forced a rollback in competitors' price hikes by refusing to go along. Respondent obviously disputes these contentions, claiming that independent market forces influenced its specific pricing decisions and that the Executive Committee did not adopt the Task Force pricing recommendations.

The evidence of DuPont's cost advantage and its pricing behavior clearly indicates that it exercised some degree of price leadership in the industry. For example, internal company documents reveal DuPont's own belief in 1975 that if price increases were to occur it would have to lead the way. (CX 99A) Moreover, DuPont's ability to force a rollback of price hikes in early 1975, to initiate successfully a lesser price increase several months later, and to force further rollbacks in 1976 and 1977, points strongly to the conclusion that respondent had a measure of power over price.

It is true, of course, as respondent contends, that other factors influenced industry pricing between 1972 and 1978, factors which suggest that DuPont did not have unfettered control over prices. Because of a shortage, DuPont was unable to roll back prices in 1972,

thereby creating a two-tiered pricing structure. DuPont's actions in forcing price rollbacks in later years can be explained, as respondent contends, by independent market forces such as excess capacity, customer reaction and the threat of imports. Customers, for example, could reduce their consumption of TiO_2 to some extent through the use of extenders. And, as long as excess capacity existed, competitors had an incentive to increase sales by discounting in order to reduce fixed costs. By DuPont's own account, it gained market share early in the slump through aggressive pricing but suffered a slippage later when prices were kept too high. (CX 182C) Thus, there were some constraints on DuPont's pricing decisions, but that does not detract from the fact that respondent enjoyed significantly greater freedom than its rivals to influence industry pricing.

As for the Task Force recommendations concerning deterrent or limit pricing, it is hard to reach any conclusion other than that such an objective was part and parcel of the overall growth strategy. To be sure, the 1972 plan presented to the Executive Committee did not expressly refer to a limit pricing policy. Nevertheless, that objective was viewed by the Task Force in 1975 as an element of the plan and later Task Force reports reiterated this feature. (CX 91H, 76D) Had the Executive Committee rejected such an approach, it seems highly unlikely that it would have surfaced in later reports. But, having found that such a pricing strategy existed, it is quite another thing to ascertain how it affected specific pricing decisions. In fact, in light of the other market factors affecting DuPont's specific pricing decisions, it is impossible to discern from the record the degree to which DuPont looked to competitors' expansion plans in making those decisions. There is no evidence, however, that DuPont priced below its costs and complaint counsel do not attempt to make such a showing. [18]

In view of the pricing evidence, it is quite probable that complaint counsel's and respondent's seemingly contradictory positions are, in fact, not inconsistent. As noted earlier, DuPont had performed several calculations of pricing parameters, including the limit price above which competitors could be expected to bring in new capacity. But, because general economic forces kept demand below anticipated levels and put downward pressure on TiO_2 prices during the period in question, DuPont and its competitors may well have been pricing in an area below the limit price, *i.e.*, the price that, in the growing market of 1972, would suffice to deter competitive expansion. In such a situation, DuPont apparently would be less concerned about the critical expansion-inducing price and more concerned with short-

term market share gain or loss, especially as it affected the efficient utilization of existing capacity. This is not to suggest, of course, that DuPont's pricing responses in 1975–77 had no impact on competitors' expansion plans. To the extent rivals were denied price hikes by DuPont, their profits undoubtedly suffered, thereby making it even less likely that new expansion would be contemplated. What the evidence does suggest, however, is that the pricing decisions of DuPont during this period may well have reflected short-term market conditions more than long-term strategic considerations.[11] Nevertheless, while DuPont did not have absolute control over price and was constrained by market forces beyond its control, there is persuasive evidence that it was able to exert its influence over the prices of competitors and that it sought to do so for the dual purpose of generating sufficient funds for its own expansion and depriving competitors of sufficient funds to expand. This pricing behavior is analyzed below in light of current standards of predation and exclusionary conduct.

Finally, as with the expansion-deterring price issue, respondent also attempts to insulate its Executive Committee from association with the long-run welfare considerations developed by the Task Force in 1975 for the purpose of comparing the "growth" and "maintain" strategies. While the Executive Committee did not set prices, it was certainly aware of the basis for the Pigments Department pricing decisions. It also seems clear from the presentations to the Executive Committee that it knew that under the prevailing price structure competitors had not come forward with expansions. Finally, in connection with its decision in 1975 [19]not to delay De Lisle, the record demonstrates that the Committee received information showing a price differential between the two alternative strategies (CX 116M), and it was aware that the long-run superior profitability of the De Lisle alternative became apparent only after the third year of projection. However, it appears that the projected superiority of the De Lisle alternative was based, to a considerable degree, on the higher sales volume and the avoidance of excess industry capacity associated with that alternative. The presentation to the Executive Committee did indicate that a higher market share had "value," but that term had several meanings (Tr. 1455, 1468), and it is not clear what DuPont personnel concluded about such

[11] In addition, because of DuPont's cost advantage, it is quite logical to assume that the cost pressures inducing respondent's competitors to raise prices did not affect DuPont as severely. In the oligopolistic TiO_2 market, DuPont's competitors might have hoped and expected that other firms would go along with price hikes, even in the face of slumping demand, and such action might appear rational. But, in view of DuPont's lower costs, its refusal to go along with the price increases seems consistent with explanations that are not based solely on deterrence considerations.

value. From the welfare analysis we can tell that if De Lisle were delayed, uncoordinated competitive expansions might drive the price of TiO_2 down for a period of time, perhaps at some temporary social cost because of inefficient capacity utilization, whereas if De Lisle were built DuPont would probably enjoy an even greater degree of price leadership. But the predictions of the Task Force do not reveal the extent to which DuPont would attempt to exercise its market power in the future.

In sum, the facts show rather unequivocally that DuPont, with a 30% market share in 1972 and a substantial cost advantage over its rivals, sought to exploit this opportunity by embarking on a long-term expansion project to capture the demand growth anticipated over the following decade. In pursuing this objective, DuPont foresaw that this plan would significantly enhance its market share, possibly giving the firm a 65% share by 1985. In addition, DuPont took into account the impact of its actions on expansion by competitors, with particular emphasis on the effects of its pricing decisions and the competitive consequences of delaying De Lisle when the market turned downward in the mid-1970s. At the same time, DuPont's pricing and construction decisions were also influenced by intervening market factors. Lastly, DuPont refused to license its technology, preferring instead to reap the rewards of its low cost technology by direct application rather than by sharing it with competitors.

Whether this conduct violates the antitrust laws is the critical issue to which we turn next. [20]

Legal Discussion

Complaint counsel argue that DuPont's output expansion, its timing of that expansion, its pricing policies and its refusal to license technology were carried out with the objective of attaining a monopoly share of the TiO_2 market, and that the plan, if not already successful, is close to the mark. In urging a finding of liability, complaint counsel rely principally on traditional attempted monopoly analysis, and they contend that DuPont's conduct was unreasonably exclusionary, using a rule-of-reason approach.

It is alleged that this expansion program is unlawful only if taken in its entirety. Complaint counsel admit that no one element of the aforementioned conduct in DuPont's strategy is sufficiently unreasonable to be unlawful if taken independently. Rather, their theory is that the elements combine to create an unreasonably exclusionary

effect, thereby constituting an attempt to monopolize and an unfair method of competition under Section 5 of the FTC Act.[12] Complaint counsel stress that DuPont's expansion plan "made no sense unless it results in a monopoly" (Tr. OA 17), and that its conduct foregoes short-run profits and is profit-maximizing in the long run "*only* if competition is stifled and monopoly can be achieved." (CRB 36) (emphasis in original)

This case raises fundamental questions about the extent to which dominant firms may aggressively pursue competitive opportunities, especially where they enjoy some form of cost or technological advantage over their rivals. More specifically, the crucial issue facing us is not whether such firms may legitimately compete or capitalize on their advantages, but whether those opportunities are exploited in an unreasonable fashion. In other words, how much latitude should be afforded a major, well-established firm when it seizes a competitive edge and attempts to enhance significantly its market position? In the context of this case the question is not so much whether DuPont had the right to expand but whether it did so by measures that went beyond what were justified by its cost advantage.

a) *Section 2 Standards*

We begin our discussion by focusing on Section 2 of the Sherman Act, 15 U.S.C. 2, which makes it unlawful for any person to monopolize, or attempt to monopolize, any part of [21]the trade or commerce among the several states.[13] Section 5 of the Federal Trade Commission Act empowers the Federal Trade Commission to prohibit certain unfair methods of competition, and that section has been construed to cover conduct that violates either the prohibitions of the Clayton Act and the Sherman Act or conduct that could lead to unreasonable restraints on competition if not prohibited. *FTC* v. *Brown Shoe,* 384 U.S. 316, 321 (1966); *FTC* v. *Cement Institute,* 333 U.S. 683 (1948).

The classic definition of the offense of attempt to monopolize is set forth in *Swift & Co.* v. *United States,* 196 U.S. 375, 396 (1905):

> Where acts are not sufficient in themselves to produce a result which the law seeks to prevent—for instance, the monopoly—but require further acts in addition to the mere

[12] Complaint counsel also contend that Section 5 can reach practices not covered by Section 2 of the Sherman Act. (CAB 41-42) However, the case was tried principally under a Section 2 theory and we shall approach the issues from that perspective.

[13] There is no dispute as to the relevant product or geographic markets in this case. (IDF 5) The parties are also in agreement that product market shares for purposes of this case are to be determined by domestic shipments of TiO_2. (ID 9)

forces of nature to bring that result to pass, an intent to bring it to pass is necessary in order to produce a dangerous probability that it will happen.

As the Supreme Court later indicated, an attempt requires more than intent to do acts that tend toward monopoly; the intent spoken of in *Swift* is a specific intent to destroy competition or achieve monopoly. *Times-Picayune Publishing Co.* v. *United States,* 345 U.S. 594, 626 (1953); *see also* L. Sullivan, Handbook of the Law of Antitrust 135 (1977).[14] [22]

As further refined by the courts, the attempt offense includes three principal elements: (1) specific intent to control prices or destroy competition, (2) exclusionary or anticompetitive conduct, and (3) a dangerous probability of success. *E.g., California Computer Products, Inc.* v. *IBM Corp.,* 613 F.2d 727, 736 (9th Cir. 1979); *Pacific Engineering & Production Co. of Nev.* v. *Kerr-McGee Corp.,* 551 F.2d 790, 791 (10th Cir. 1977); *Central S. & L. Ass'n of Chariton, Iowa* v. *Federal Home Loan Bank Board,* 422 F.2d 504, 508 (8th Cir. 1970); *Merit Motors, Inc.* v. *Chrysler Corp.,* 417 F.Supp. 263, 269–270 (D.D.C. 1976), aff'd., 569 F.2d 666 (D.C. Cir. 1977). These criteria, however, are not mutually exclusive but rather are interrelated to the extent that evidence of conduct may shed light on intent and the probability of success; conversely, evidence of a respondent's purpose may reveal the extent to which there are legitimate business justifications underpinning the respondent's conduct. *See Janich Bros., Inc.* v. *America Distilling Co.,* 570 F.2d 848, 853 (9th Cir. 1978), *cert. denied* 439 U.S. 829 (1978); *Transamerica Computer Co., Inc.* v. *IBM Corp.,* 481 F.Supp. 965, 989 (N.D. Cal. 1979).

With respect to the "dangerous probability" issue, there is conflict in the law as to what degree of market power, or proximity to monopoly status, need be shown before a finding of liability can be made. *Compare Greyhound Computer Corp., Inc.* v. *IBM Corp.,* 559 F.2d 488, 496, 504 (9th Cir. 1977),[15] and *Kearney & Trecker Corp.* v. *Giddings & Lewis, Inc.,* 452 F.2d 579, 598 (7th Cir. 1971), *cert. denied* 405 U.S. 1066 (1972), with *United States* v. *Empire Gas Co.,* 537 F.2d 296, 305 (8th Cir. 1976), *cert. denied* 429 U.S. 1122 [23](1977).[16] Suffice

[14] Complaint counsel do not allege that DuPont's conduct is designed to destroy its rivals; rather, they urge that destruction of rivals is unnecessary to the success of predatory strategy, Complaint Counsel Appeal Brief, 50, when merely preventing rivals from competing in the short run enables a predator to attain long-run monopoly power. See O. Williamson, Williamson on Predatory Pricing II, 88 Yale L. J. 1183, 1185 (1979). We agree with this position as a general proposition. As the Court observed in *United States* v. *Griffith, et al.,* 334 U.S. 100, 107 (1948), "[t]he antitrust laws are as much violated by the prevention of competition as by its destruction."

[15] In fact, the Ninth Circuit has essentially dispensed with the dangerous probability requirement as an independent element of the attempt offense, saying instead that the probability of success is important only as evidence of specific intent. That appears, however, to be a minority view among the circuits, and for purposes of our discussion we assume that some showing of a dangerous probability of success is required.

[16] The recent report of the National Commission for the Review of Antitrust Laws and Procedures expresses concern about construing the "dangerous probability" standard too stringently, so that liability attaches only if the

(Continued)

it to say, the evidence here of DuPont's leading position in 1972, its substantial cost advantage, its price leadership, and the existence of substantial scale economies indicates that respondent was on the verge of achieving monopoly power and that even the more stringent "dangerous probability" test appears to have been met. That is also the view of the ALJ. (ID 44)

We turn next to the issue of "specific intent," an elusive aspect of the attempt offense. In this connection, it seems important to bear in mind what the attempt doctrine does not proscribe. As Areeda & Turner put it:

> "specific intent" clearly cannot include . . . the mere intention to prevail over one's rivals. To declare that intention unlawful would defeat the antitrust goal of encouraging competition on the merits, which is heavily motivated by such an intent. P. Areeda & D. Turner, *Antitrust Law* ¶822a at 314 (1977) (footnote omitted)

Similarly, Professor Cooper observes that:

> Plainly, then, the "specific intent" required in attempt cases is not simply a subjective intent to prevail in the market. Instead, it is the intent to indulge in means that are in some sense untoward. Cooper, *Attempts and* [24]*Monopolization: A Mildly Expansionary Answer to the Prophylactic Riddle of Section Two,* 72 Mich. L. Rev. 373, 395 (1974) (footnote omitted)[17]

We highlight the intent issue because complaint counsel in their appeal and reply briefs make much of the documentary evidence concerning DuPont's 1972 goal of capturing a 56% market share by 1980 (and possibly 65% by 1985) and other statements indicating DuPont's awareness of the potential effects on competitors of its expansion plan. (CAB 44–45; CRB 22) It is argued that these documents demonstrate a "specific intent" to exclude competition and gain a monopoly. In fact, complaint counsel contend that this evidence of intent (together with a dangerous probability of success) is sufficient to establish liability even without looking to conduct.

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respondent or defendant has a near-monopoly share of the market. Instead, the Commission, citing the *Kearney* decision, urged a balancing approach that gives less weight to market power considerations where the challenged conduct is clearly anticompetitive. National Commission for the Review of Antitrust Laws and Procedures, *Report to the President and the Attorney General* 145–49 (January 22, 1979). We share some of these concerns and note that if market share is the governing factor, DuPont had only about a 30% market share in 1972 when it embarked on its expansion program. Yet, the evidence clearly reveals DuPont's capability and desire to increase its market share to levels that, at least, approach monopoly proportions. While we ultimately cannot find DuPont's conduct to be unreasonable, our disposition of this matter should not depend upon a showing that DuPont's market position exceeded some magic market power (as measured by market share) criterion.

[17] Even Professor Sullivan, who rejects an overly restrictive interpretation of Section 2, has this to say about specific intent:

> It also seems clear that an intent to monopolize could not be inferred merely from conduct consistent with efficient competitive responses, such as merely expanding to meet new opportunities. Even though such conduct would, on the most sweeping view of the law, suffice for the offense of monopolization if monopoly power were in fact achieved, such conduct does not warrant an inference of specific intent to monopolize. L. Sullivan, *Handbook of the Law of Antitrust,* 136 (1977) (hereinafter cited as Sullivan).

But intent is a barren issue without consideration of the means contemplated for acquiring monopoly power. It is simply unrealistic to divorce conduct from intent. Even the broad language of *Alcoa,* [18] which complaint counsel quote (CAB 43), focuses primarily on Alcoa's conduct and its effect on competition. And, of course, that was a monopolization case, which involves the less demanding general intent test.

As a general matter, it seems unwise to find that a firm has the requisite specific intent for anticipating the exclusionary consequences of successful competitive behavior which leads, or may lead, to a monopoly, so long as that behavior is reasonable. To suggest otherwise would be to proscribe all acts in which firms [25]conjure up some thoughts of achieving monopoly irrespective of the actual character of the means employed to gain that end. Perhaps the relationship between intent and conduct is best characterized by the court in *Transamerica:*

> More than an intent to win every sale, even if that would result in the demise of a competitor, is required before it can be concluded a defendant has the type of exclusionary intent condemned by the antitrust law. Intent and conduct are closely related; and there must be some element of unfairness in the conduct before an anticompetitive intent can be found, as distinguished from the benign intent to beat the opposition. (citations omitted) 481 F.Supp.at 1010.

There is no doubt that intent can shed light on questionable conduct and the justifications for the conduct.[19] But the crucial issue is whether DuPont's conduct represents legitimate competitive behavior or an unreasonable effort to propel the firm into a dominant position in the TiO_2 market. That is the issue to which we address the bulk of our discussion.

We come now to the critical element of an attempt to monopolize for purposes of this case: the reasonableness of DuPont's conduct in formulating and executing its expansion strategy. Few antitrust issues of late have sparked more interest and debate than has the subject of predation and strategic deterrent behavior. At stake is the extent to which dominant firms should be permitted to compete aggressively, and the standards by which conduct should be deemed predatory (and therefore unreasonable). These issues [26]have

[18] *United States* v. *Aluminum Company of America,* 148 F.2d 416 (2d Cir. 1945).

[19] As Judge Friendly observed in *Buffalo Courier-Express, Inc.,* v. *Buffalo Evening News, Inc.,* 601 F.2d 48, 54 (2d Cir. 1979), in discussing the relationship between intent and conduct:

> The intent alone is not sufficient, although, of course, it may give color to the acts. Similarly, acts alone are insufficient, although they may evidence intent.

received extensive discussion in recent court decisions and economic literature,[20] and complaint counsel's case draws heavily from this debate.

Central to complaint counsel's definition of predation is the notion that a firm in trying to discipline or destroy competition will sacrifice short-term gain for long-term competitive advantage. Professor Sullivan provides a good summary of this point in the following excerpt from his treatise:

> the predator seeks *not to win the field by greater efficiency,* better service, or lower prices reflective of cost savings or modest profits. The predatory firm tries to inhibit others in ways *independent of the predator's own ability to perform effectively* in the market. Its price reduction or predatory expenditure is calculated to impose losses on other firms, not to garner gains for itself; indeed, the predation is likely to involve present losses to the predator, or at all events to foreclose profits which could currently be earned, detriments which are accepted by the predator as the cost of freeing itself for the future from the competition it now faces. Sullivan at 111. (footnotes omitted) (emphasis added) [27]

This description seems sound, but the short-term/long-term dichotomy can only be carried so far, for otherwise, any action by a monopolist to compete by ways that are not profit-maximizing in the short-run would be suspect.[21]

It is within this context that we review the relevant judicial precedent and economic literature. Although no case has dealt directly with the unique combination of activities present here, several decisions have touched on various aspects of the conduct engaged in by DuPont. These involve cases of alleged monopolization as well as attempted monopolization. It is, of course, axiomatic that the duty imposed on a monopolist may not be incumbent on a lesser firm, even a substantial industry leader. Nevertheless, a review of the principles governing conduct by monopolists is desirable for two reasons. First, the standards for judging attempts to monopolize are derived in part from the standards applicable to the completed offense. Second, the courts have historically been suspicious of excessive market power in the hands of private firms and have interpreted the offense of monopolization to include conduct by

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[20] Areeda & Turner, Predatory Pricing And Related Practices Under Section 2 of the Sherman Act, 88 Harv. L. Rev. 697 (1975); Scherer, Predatory Pricing and the Sherman Act: A Comment, 89 Harv. L. Rev. 868 (1976); Areeda & Turner, Scherer on Predatory Pricing: A Reply, 89 Harv. L. Rev. 891 (1976); Scherer, Some Last Words On Predatory Pricing, 89 Harv. L. Rev. 901 (1976); Williamson, Predatory Pricing: A Strategic And Welfare Analysis, 87 Yale L. J. 284 (1977); Spence, Entry, Capacity, Investment and Oligopolistic Pricing, 8 Bell J. of Econ. 534 (1977); Williamson, Williamson On Predatory Pricing II, 88 Yale L. J. 1183 (1979); Schmalensee, On the Use of Economic Models In Antitrust: The *ReaLemon* Case, 127 Pa. L. Rev. 994 (1979); Baumol, Quasi-Permanence of Price Reductions: A Policy for Prevention of Predatory Pricing, 89 Yale L. J. 1 (1979); Joskow & Klevorick, A Framework for Analyzing Predatory Pricing Policy, 89 Yale L. J. 213 (1979).

[21] Sullivan, in distinguishing between legitimate and unlawful behavior, further suggests that predatory conduct is likely to seem "odd," "jarring" or "unnatural." "It will not strike the informed observer as normal business conduct, as honestly industrial." Sullivan at 111–12.

companies whose market shares fall far short of 100 percent control. As such, the range of permissible behavior for monopolists and non-monopolists cannot always be sharply differentiated, especially at the margin. In view of these factors and DuPont's close proximity to monopoly status, an examination of some of the relevant monopoly decisions seems particularly pertinent.

It should be noted at the outset that we are not dealing here with conduct that amounts to an unlawful restraint under Section 1 and, as such, an attempt to monopolize under Section 2. *See United States* v. *Columbia Steel Co.,* 334 U.S. 495, 525 (1948); *United States* v. *Griffith,* 334 U.S. 100, 106 (1948); *United States* v. *United Shoe Machinery Corp.,* 110 F.Supp. 295, 342 (D. Mass. 1953). Rather, we are concerned with single-firm conduct, the lawfulness of which is more ambiguous and depends on a variety of factors including the market position of the respondent, the structure of the industry, the nature of the conduct (and alternatives to such conduct), and the effect of the conduct on competition. Thus, we agree with complaint counsel that it is appropriate to employ a rule of reason-type approach for judging the lawfulness of DuPont's behavior. [28]

Such an approach is reflected even in the far-reaching, landmark decision in *United States* v. *Aluminum Company of America,* 148 F.2d 416 (2d Cir. 1945) ("*Alcoa*"), the progenitor of the cases on exclusionary expansion, as well as complaint counsel's theory here. In that case Alcoa, with its 90 percent market share, confronted rivals with repeated increases in capacity in anticipation of demand, thereby excluding competitors from profitable opportunities to grow. In condemning this action and finding that Alcoa was not the "passive beneficiary of a monopoly," Judge Hand nonetheless concluded that not all monopolies were proscribed by Section 2. In addition to natural monopolies and those created by "force of accident," he cited the situation where "[a] single producer may be the survivor out of a group of active competitors merely by virtue of his superior skill, foresight and industry." *Id.* at 430. Thus, Judge Hand felt that some evaluation of the justifications for the monopolist's behavior and the resulting market structure was called for, although, as applied to Alcoa, he believed that its capacity expansions were not "inevitable" and that they did not reflect the actions of firms "who do not seek, but cannot avoid, the control of a market." *Id.* at 431.

In *United Shoe Machinery,* Judge Wyzanski pointed out that Section 2 clearly covered common law restraints of trade and clearly did not cover market control captured solely through superior skill and intelligence. As to the intermediate case, he observed that the

legislative history was silent as to the legal consequences of monopolies which reflect neither of the above causes but stem rather from "some practice which without being predatory, abusive, or coercive was in economic effect exclusionary." 110 F.Supp.at 341.

Relying heavily on the legal tests set forth in *Alcoa* and *Griffith*, Judge Wyzanski found that United Shoe's practices were exclusionary and not economically inevitable. In so doing he elaborated on the exception to liability for monopolization formulated by Judge Hand:

> the defendant may escape statutory liability if it bears the burden of proving that it owes its monopoly solely to superior skill, superior products, natural advantages, (including accessibility to raw materials or markets), economic or technological efficiency, (including scientific research), low margins of profit maintained permanently and without discrimination, or licenses conferred by, and used within, the limits of law, (including patents on one's own inventions, or franchises granted directly to the enterprise by a public authority). *Id.* at 342.

[29]Applying this to United Shoe's leasing practices, Judge Wyzanski determined that:

> they are not practices which can be properly described as the inevitable consequences of ability, natural forces, or law. They represent something more than the use of accessible resources, the process of invention and innovation, and the employment of those techniques of employment, financing, production, and distribution, which a competitive society must foster. *They are contracts, arrangements, and policies which, instead of encouraging competition based on pure merit, further the dominance of a particular firm. In this sense, they are unnatural barriers; they unnecessarily exclude actual and potential competition; they restrict a free market. Id.* at 344–45. (emphasis added)

Turning briefly to *Griffith*, there is language in that case that could be construed to proscribe virtually any monopoly, however acquired or maintained.[22] Yet, the Court went on to emphasize that it is the "exercise" or "use" of monopoly power to foreclose competition or gain a competitive advantage that is unlawful, thereby suggesting that for a violation to exist there must be something more than the exercise of inherent competitive advantages, such as technological advantages. The facts of that case required little analysis of competitive trade-offs as the practices at issue there—concerted efforts by film exhibitors to utilize monopoly power in some markets to gain exclusive distribution rights in other markets—revealed significant competitive harm with little or no offsetting justifica-

[22] As put by the Court, "monopoly power, whether lawfully or unlawfully acquired, may itself constitute an evil and stand condemned under Section 2 even though it remains unexercised. For Section 2 of the Act is aimed, *inter alia*, at the acquisition or retention of effective market control. See *United States* v. *Aluminum Co. of America*, 2 Cir., 148 F.2d 416, 428, 429." *United States* v. *Griffith*, 334 U.S. 100, 107 (1948) (footnote omitted). In citing *Alcoa*, it is not clear whether the Court was endorsing Judge Hand's test or embracing a somewhat different formulation.

tions. Indeed, the Court called these practices a "misuse of monopoly power" and found violations of both Sections 1 and 2 of the Sherman Act. 334 U.S. at 108.

Finally, in the most recent Supreme Court monopoly decision, *United States* v. *Grinnell,* 384 U.S. 563 (1966), the Court restated the test for monopolization as one which, in part, proscribes the "willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident." *Id.* at 570–71. However, [30] as in *Griffith,* the Court was not called upon to draw any subtle distinctions between permissible and impermissible monopoly conduct, since the tactics employed there to attain market control, primarily a series of acquisitions, constituted a rather clear case of unjustified behavior, which might have given rise to a separate violation under Section 7 of the Clayton Act.

Thus, these decisions reflect at least a general judicial willingness to weigh the relative competitive virtues and evils of dominant firm behavior even in the monopoly context. With the exception of *Alcoa,* however, the facts of the other cases and the broad principles set forth therein provide only the most general sort of guidance in analyzing the lawfulness of DuPont's activities. As noted above, *Grinnell* and *Griffith* involved factual situations where there was little doubt about the anticompetitive nature of the challenged behavior. *United Shoe* raised more difficult issues, but as the court noted there, the leasing system in question, while not an unusual marketing tool, heightened entry barriers substantially and introduced no significant competitive efficiencies or other benefits.

As for *Alcoa,* it superficially at least provides a much closer analogy to the facts of this case. But there are differences, not the least of which is the fact that Alcoa was a monopolist that had maintained its hold over the market through repeated additions to capacity over a long period of time.[23] Moreover, the circumstances and justifications surrounding those increases in output are not detailed. In light of more recent precedents and literature on exclusionary conduct, discussed below, *Alcoa* leaves unanswered a number of important questions that are especially relevant in the context of the attempt case now before us.[24]

For example, *Alcoa* reveals nothing about the scale economies

[23] Areeda & Turner in their treatise suggest that a better rationale for the holding in *Alcoa* would have been to construe Section 2 to outlaw persistent monopolies, subject to certain efficiency defenses such as economies of scale or superior skill. P. Areeda & D. Turner, Antitrust Law at ¶623b. Whether Section 2 of the Sherman Act or Section 5 of the FTC Act reach that far is an issue we need not decide here.

[24] For a general critique of the *Alcoa* decision, see P. Areeda & D. Turner, Antitrust Law at ¶608; Sullivan at 95–97.

inherent in Alcoa's expansions, nor does the decision specifically address whether Alcoa's additional output conformed to demand [31] estimates or resulted in excess capacity. Furthermore, while the court condemned Alcoa's repeated additions to capacity as preemptive and preservative of monopoly, it gave unclear signals about other aggressive conduct engaged in by the firm, some of which it found to be reasonable and justified by legitimate business reasons.[25] Whatever may have been the proper result under the facts in *Alcoa,* we believe these issues need to be explored in greater depth in the context of an attempt to monopolize, such as we have here.

The attempt cases encompass a wide variety of challenged conduct and the courts have employed various approaches in assessing the reasonableness of defendants' actions. *See generally* Hawk, *Attempts to Monopolize—Specific Intent as Antitrust's Ghost in the Machine,* 58 Cornell L. Rev. 1121 (1973). For example, where the conduct at issue reveals a clear purpose to destroy competition, with no countervailing business justifications, the Supreme Court has had little difficulty in declaring such behavior predatory. Thus, in *Lorain Journal Co.* v. *United States,* 342 U.S. 143, 153 (1951), the sole newspaper in the market incurred liability for attempting to monopolize by its refusal to accept advertising orders from merchants who patronized a competing radio station. By contrast, in *Times-Picayune Publishing Co.* v. *United States,* 345 U.S. 594, 627 (1953), the Court found no attempt to monopolize in conduct that was "predominantly motivated by legitimate business aims." The defendant, a newspaper publisher with a monopoly morning paper and an evening paper facing competition, adopted a unit pricing plan requiring advertisers to purchase advertising in both its papers, a practice which allegedly foreclosed the competing [32]evening paper from a share of the advertising market. While resting its decision on the absence of specific intent, the Court appeared to draw upon its earlier Section 1 analysis of the advertising plan in finding a proper business purpose. Under that analysis, the Court found the plan reasonable, noting that many other publishers had adopted similar

[25] It is instructive to note that the Government sought to show that many of Alcoa's transactions, "neutral on their face, were not in fact necessary to the development of Alcoa's business, and had no motive except to exclude others and perpetuate its hold upon the ingot market." Specifically, the Government attempted to prove that Alcoa bought up bauxite deposits and water-power sites "not for the purpose of securing an adequate future supply, but only in order to seize upon any available supply and so assure its monopoly." The court viewed the charge as depending entirely upon Alcoa's intent, "for if the purchases provided for the future needs of the business, or for what Alcoa honestly believed were its future needs, they were innocent." 148 F.2d at 432–33. The district court believed the lengthy testimony of Alcoa officials that Alcoa had not purchased the bauxite and water-power sites in order to exclude others, and the reviewing court upheld that belief, even though Alcoa "did buy a number of such sites which it did not fully use." *Id.* at 434. This determination reflects the tension that exists in distinguishing exclusionary behavior from conduct that is undertaken for legitimate, non-predatory business purposes but which may have incidental exclusionary effects.

plans and that unit rates substantially reduced overhead costs. *Id.* at 633. On balance, however, the decision provides only limited guidance as to the role and weight to be accorded conduct evidence in evaluating intent, especially where the conduct falls short of a Section 1 violation.

In a case involving allegations of preemptive expansion, *American Football League* v. *National Football League,* 323 F.2d 124 (4th Cir. 1963), the court determined that the NFL's plans to offer franchises in two new cities in 1960, the same year that the AFL started up, did not constitute an attempt to monopolize. Focusing heavily on the issue of intent, the court found that the NFL had independent business reasons for expanding and had planned to do so even prior to the formation of the AFL. The two-city expansion, according to the court, was simply the implementation of those earlier plans and the NFL would have been "greatly embarrassed" if it had not followed through. *Id.* at 132.

A different result, however, was reached in *Philadelphia World Hockey Club* v. *Philadelphia Hockey Club,* 351 F.Supp. 462 (E.D. Pa. 1972), a monopolization case, in which the National Hockey League's expansion efforts were cited as evidence of a wrongful intent to monopolize the market for major league professional hockey players. While relying on *Alcoa,* the court nevertheless recognized that the creation of the WHL and the NHL's expansion drive were "both responses to an increased market for those entering as well as those already in the field." *Id.* at 512. In finding liability the court indicated that it did not rely solely on expansion but took account of other conduct, such as the reserve clause, and statements by the NHL President expressing a clear determination to preserve the NHL as the exclusive major professional hockey league in the United States and Canada. *Id.* at 512–13. Thus, in view of this analysis, it is not entirely clear what the court would have done had it been faced with the kind of growth plan encountered here: expansion that is consistent with demand projections and can be accomplished only through large, efficient-scale operations which have the inevitable tendency of restricting competitors' efforts to expand at scale.[26] [33]

In *Bergjans Farms Dairy Co.* v. *Sanitary Milk Producers,* 241 F. Supp. 476 (E.D. Mo. 1965), *aff'd* 368 F.2d 679 (8th Cir. 1966), the court

[26] In addition to *Alcoa* and *Philadelphia Hockey Club,* complaint counsel also cite *Schine Chain Theatres, Inc.* v. *United States,* 334 U.S. 110, 119 (1948), as supporting generally their position. But in *Schine,* the Supreme Court affirmed findings that *Schine* threatened to open new theatres in towns where competitors refused to sell out or where new entry was planned. It appears that the essence of the activity under scrutiny there—disciplining rivals rather than responding to long-run market opportunities—is substantially different in nature from the conduct at issue here.

found an attempt to monopolize from an overall course of conduct that included expansion by acquisition coupled with other restrictive conduct. There, a dairy cooperative that produced 55-60 percent of the raw milk in a market sought to increase the percentage of its milk purchased as higher-priced "Class I" milk by processors and concurrently to exclude other producers from such sales. To accomplish its goal, the cooperative employed price cuts, false pricing announcements, secret discounts, acquisition of a processor and predatory price cuts on processed milk. As an integrated firm, it forced other processors to buy Class I milk from its members, employing such tactics as below-cost sales, price discrimination and subsidization, and price-fixing with retail stores. It is not clear, however, how much weight the court gave to each of the practices, and the conduct, including the nature of the expansion, differs considerably from the behavior of DuPont.

By contrast, internal expansion, without more did not constitute an attempt to monopolize in *Hiland Dairy, Inc.* v. *Kroger Co.*, 402 F.2d 968 (8th Cir. 1968), *cert. denied*, 395 U.S. 961 (1969). In that case, the plaintiff sought to enjoin Kroger from building a dairy processing plant with the capacity to supply more than 20 percent of total demand, claiming that building the plant constituted an attempt to monopolize and that the expansion would give Kroger power to impose unreasonable restraints on competition. No conduct involving unreasonable restraints was at issue, nor was Kroger a dominant firm in the market. The court distinguished *Alcoa*, citing the "unique" factors present in that case—a 90 percent market share and repeated increase in demand—and concluded that the mere act of building a plant is not by itself unfair or predatory.

In two other recent attempt cases, the practices accompanying internal expansions were not deemed to be sufficiently unreasonable to make out violations of Section 2. In one, the conduct involved unfair claims to advertisers and a promotional giveaway which apparently incurred no losses. *Buffalo Courier Express, Inc.* v. *Buffalo Evening News, Inc.*, 601 F.2d 48 (2d Cir. 1979). And, in another, low pricing to increase demand did not render illegal a firm's doubling of its capacity, since the new capacity was installed in anticipation of its future need and was not to be carried at a loss. *Structure Probe, Inc.* v. *Franklin Institute*, 450 F. Supp. 1272, 1288 (E.D. Pa. 1978), *aff'd mem.* 595 F.2d 1214 (3d Cir. 1979). **[34]**

These cases, like the monopolization cases discussed above, unfortunately are of limited usefulness to the task here. They provide no clear explication of the factors to be considered in assessing the reasonableness of conduct by firms with market power approaching

monopoly proportions. For the most part, the courts have couched their decisions in terms of such general considerations as the defendants' conformity with prevailing business norms or the existence of independent economic justifications to support the challenged conduct. Insofar as the expansion cases are concerned, about the most that can be said is that the courts appear to be cautious about condemning expansion by non-monopolists, especially where the expansion is not accompanied by other conduct that is anticompetitive.

In addition to these cases, however, several decisions of late, cited by respondent, address the reasonableness of dominant firm behavior in greater depth. Although these decisions do not involve the kind of output expansion activity present here, they do shed further light on the conduct standards applicable to both monopolization and attempted monopolization cases.

Of particular interest is a series of cases involving the marketing practices of IBM. *California Computer Products* v. *IBM Corp.* ("Cal Comp"), 613 F.2d 727 (9th Cir. 1979); *Greyhound Computer Corp.* v. *IBM Corp.*, 559 F.2d 488 (9th Cir. 1977); *ILC Peripherals* v. *IBM Corp.* ("Memorex"), 555 F.2d 1379 (9th Cir. 1977); *Telex Corp.* v. *IBM Corp.*, 510 F.2d 894 (10th Cir. 1975); *Transamerica Computer Co.* v. *IBM Corp.*, 481 F. Supp. 965 (N.D. Cal. 1979). Among the various charges of exclusionary conduct were allegations that IBM lowered prices to drive competitors from the market and preserve its market share, altered its leasing policies in order to frustrate and exclude competitors, and implemented superfluous design changes in equipment to forestall competition.

In finding IBM's actions to be reasonable, the court in *Cal Comp* concluded that IBM's dominant position in computers resulted initially from technological superiority, and that the firm was entitled to maintain that position through "shrewdness in profitable price competition," which the court characterized as business acumen. 613 F.2d at 742. In addition to finding IBM's price reductions "highly profitable,"[27] the court also found the design changes [35]to be cost-saving technical improvements which justified lower prices. According to the court, IBM, even as a monopolist, had the right to redesign products to reduce cost or improve performance, and the firm was under no obligation to predisclose its new technology to competitors. *Id.* at 744.

Addressing somewhat different leasing and pricing policies in

[27] While adhering to the Areeda-Turner marginal cost rule as the basic test for predatory pricing, the court nevertheless indicated that under the right circumstances limit pricing might be proscribed, and that pricing above marginal or average variable costs might be condemned when viewed in light of other aspects of the monopolist's conduct. 613 F.2d at 743.

Greyhound, the Ninth Circuit upheld IBM's fixed term leasing plan as a reasonable response to competition, but reversed a directed verdict for the firm on the pricing issues, saying that the evidence showed IBM's actions to be *prima facie* anticompetitive without legitimate business purpose. 559 F.2d at 505. In reaching this result the court started with the premise that IBM, as a monopolist, "would be precluded from employing otherwise lawful practices that unnecessarily excluded competition from the [market]." *Id.* at 498. Applying this standard, the court determined that changes in the technological discount offered by IBM would not be economically justified except as a means of inhibiting leasing company competitors. Similarly, the court found that IBM's action in boosting maintenance rates on its new generation of equipment, despite lower maintenance costs, was not competitively justified and had the primary effect of restricting competitors' access to such equipment by stretching out the period required to recoup investment.

In *Telex,* IBM's redesigned peripheral equipment and accompanying price reductions were judged by a two-fold test: (1) whether the acts were business practices typical of those used in a competitive market, and (2) whether the conduct involved the use of monopoly power. 510 F.2d at 925-26. In finding IBM's conduct to be reasonable, ordinary business behavior, the court felt that a firm such as IBM should be given sufficient latitude to respond to erosion of its lawfully acquired market share. As the court observed:

> It would seem that technical attainments were not intended to be inhibited or penalized by a construction of Section 2 of the Sherman Act to prohibit the adoption of legal and ordinary marketing methods already used by others in the market, or to prohibit price changes which are within the "reasonable" range, up or down. *Id.* at 927.

Two additional district court opinions involving IBM are worth noting. These cases also deal with conduct that is similar or identical to the practices at issue in the aforementioned cases, and both decisions devote considerable discussion to the question of predatory pricing standards. In *Memorex,* the court concluded that a two-part test should be applied to allegations of exclusionary pricing. If entry barriers are low, the Areeda-Turner marginal or average variable cost standard should hold. If entry barriers are high, the proper measure would be to determine whether prices are below short-run profit maximizing levels—in other words, the inquiry would focus on whether the defendant is sacrificing current [36]profits to gain even higher profits in the future.[28] In addition, the court felt that pricing

[28] In arriving at this position, the court relied on two Ninth Circuit appellate cases involving allegations of attempted monopolization and a Fifth Circuit case dealing with price discrimination under the Robinson-Patman

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to meet competition was permissible without regard to costs, thus allowing the dominant firm to match any competitive price offerings irrespective of the entry hurdles facing the would-be challenger. According to the court, IBM's pricing met these tests. 458 F. Supp. at 433.

As for the non-pricing conduct, the *Memorex* court found that IBM's new product offerings were significant innovations and that its product announcements were not false or misleading.

In *Transamerica,* after an exhaustive review of the precedents, the court determined that an average cost pricing test was the most defensible from an economic and public policy perspective.[29] As for design changes, the court looked to see if the changes were "unreasonably restrictive of competition," taking into account the effects on competitors and consumers, technological advantages and intent. 481 F. Supp. at 1003. In finding IBM's conduct generally reasonable, the court had this to say about the general standard for judging the behavior of a monopolist:

> Where a monopolist chooses an alternative that does not unreasonably restrict competition, the law is not offended. It is the choice of an unreasonable alternative, not the failure to choose the least restrictive alternative, that leads to liability. *Id.* at 1022. [37]

One further case deserves consideration. *Berkey Photo, Inc.* v. *Eastman Kodak Co.,* 603 F.2d 263 (2nd Cir. 1979), *cert. denied,* 100 S. Ct. 1061 (1980). Briefly, the *Berkey* court found no attempt to monopolize in Kodak's introduction of the "110" camera and no general duty of a monopolist to predisclose its innovations to competitors. Reminiscent of the charges of exaggerated and premature expansion announcements by DuPont were Berkey's allegations that Kodak made false and exaggerated claims about its new film for the 110 camera: the court disagreed, finding the film to be a superior product for which there was a market.

In reaching its decision, the court emphasized that, in the context of a monopolization case, a violation can be found only by showing the use of monopoly power. According to the court,

> a use of monopoly power is an action that a firm would have found substantially less effective, or even counterproductive, if it lacked market control. *Id.* at 291.

Act. *ILC Peripherals* v. *IBM Corp.,* 458 F. Supp. at 431-32, citing *Janich Bros., Inc.* v. *American Distilling Co.,* 570 F.2d 848, 857 (9th Cir. 1977); *Hanson* v. *Shell Oil Co.,* 541 F.2d 1352, 1358-59 (9th Cir. 1976), *cert. denied,* 429 U.S. 1074 (1977); and *International Air Industries, Inc.* v. *American Excelsior Co.,* 517 F.2d 714, 723-24 (5th Cir. 1975). These decisions, while largely endorsing the Areeda-Turner test, nonetheless suggest that pricing above average variable or total costs might be deemed to be predatory in situations where new entry is difficult.

[29] In attempt cases, however, the court, citing *Janich* and *Hanson,* n. 28 *supra,* noted that an average variable cost test might be appropriate where independent evidence of specific intent or dangerous probability is lacking. 481 F. Supp. at 989.

While reaffirming the well-established principle that actions proper for a non-monopolist may be improper if engaged in by a monopolist, the court went on to note that:

> if an action that gains a firm a competitive advantage is effective because of the company's efficiency, prestige, and innovativeness, and not because of its control over the market, the action is not a use of power. *Id.* at 291 n. 50.[30] [38]

These decisions reflect some of the most extensive efforts by the courts in recent years to devise tests for determining whether conduct by monopolists or near-monopolists is unreasonably exclusionary or constitutes legitimate competitive behavior. In so doing, the courts have fashioned a variety of criteria such as a) whether the behavior amounted to ordinary marketing practices, b) whether it was profitable or economically rational, c) whether it resulted in improved product performance or d) whether it would have been effective for a firm without market power. In addition, several of the decisions emphasize that the lawfulness of the practices depends on the market setting (*e.g.*, nature of entry barriers) and the anticompetitive potential of the challenged practices. In particular, the decisions in such cases as *Greyhound* and *Transamerica* suggest the importance of weighing the efficiencies and competitive virtues of the practices under scrutiny against their exclusionary characteristics and effects.

There is little doubt that many of these considerations can be of great help in judging the lawfulness of single-firm conduct. Actions that promote innovation or improve efficiency, for instance, should generally be encouraged, not inhibited. But we believe it would be unwise policy, especially in the face of actual or threatened monopoly, to focus solely on the benefit side of the equation while ignoring the adverse effects of dominant firm behavior. For example, a firm's conduct might consist largely of ordinary business practices, yet be highly exclusionary because of the industry structure and the firm's market power. So too, the actions of the would-be monopolist may enhance efficiency or product performance, albeit marginally, although the overall competitive effect is decidedly negative. In a similar vein, there are shortcomings in a test which relies exclusively on determining whether the conduct would have been rational for a smaller firm. On the one hand, it might be logical and necessary for a new or recent entrant to engage in below cost pricing as a

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[30] As examples of actions that may be permissible for firms with market power, the *Berkey* court had this to say:

> a firm that has lawfully acquired a monopoly position is not barred from taking advantage of scale economies by constructing, for example, a large and efficient factory. These benefits are a consequence of size and not an exercise of power over the market. Nevertheless, many anticompetitive actions are possible or effective only if taken by a firm that dominates its smaller rivals. (citations omitted) *Id.* at 274-75.

means of achieving market penetration. On the other hand, size and efficiency may coalesce so that it is difficult, if not impossible, to ascertain precisely whether an effective marketing tactic owes its success to greater efficiency or the naked exercise of market power. Moreover, behavior that is rational for a firm with little or no market power may nevertheless produce substantial and unnecessary anticompetitive effects when wielded by a firm with considerable market clout.

In the present case, DuPont's conduct appears to be justified by respondent's cost superiority over its rivals, demand forecasts and scale economies. There is no evidence that DuPont's pricing or capacity strategies were unprofitable (regardless of the cost test employed) and, as discussed later, the plant announcements do not appear to be misleading. Yet, that is not the end of our inquiry. As we have suggested, the proper test for measuring the reasonableness of DuPont's conduct takes account of overall competitive effects—pro and con—within the relevant market setting. To further explore the factors that should guide our analysis, we turn to the new literature on predatory business strategies. [39]

b) *Economic Literature*

Complaint counsel draw on recent economic literature in urging that DuPont's conduct should be condemned under a rule-of-reason approach to predation. In the process, they reject the so-called *per se* marginal cost pricing tests of Areeda and Turner and even the special *per se* rules advanced by Professor Williamson. Instead, complaint counsel support the approach suggested by Professor Scherer of looking at all relevant market factors affecting long-run welfare in determining whether dominant firm conduct is unreasonable.

Much of the current economic debate stems from the aforementioned effort by Professors Areeda and Turner to develop a set of objective, efficiency-based predatory pricing rules which will serve to deter the most likely abuses of market power and which courts can workably apply. Areeda & Turner, Predatory Pricing and Related Practices Under Section 2 of the Sherman Act, 88 Harv. L. Rev. 697 (1975). Under their proposal, only pricing below marginal or average variable costs would be deemed predatory, except where marginal costs exceed average costs; in the latter case, pricing above average costs would be legal.[31] The principal criticisms of this approach, in

[31] A significant feature of the Areeda-Turner test is the assumption that predation is most likely to occur in situations where the monopolist has excess capacity, *i.e.*, where marginal cost is less than average cost. It should also be noted that these commentators would establish no rule governing possible predatory investment in new

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the view of a number of commentators, see n. 20 *supra,* are (1) that it focuses only on eliminating equally efficient firms and ignores the social loss from elimination of less efficient firms on the ground that any other standard would chill desirable pricing behavior by firms with substantial market shares; and (2) that it fails to take account of market-place dynamics, especially the ability of dominant firms to prevent even equally efficient firms from entering the market on a viable scale. Although each of these commentators offers a somewhat different solution to the problem, they share the common objective of developing legal criteria that will adequately address the long-run welfare effects of conduct by firms having substantial market power.

Professors Scherer and Williamson, in particular, are both concerned with output decisions by dominant firms which, though not necessarily violating the Areeda-Turner cost-based rules, nevertheless serve to deter effective new entry or expansion by existing firms. Scherer, for example, criticizes Areeda and Turner for overstating the significance of predation in situations where a dominant firm maintains excess capacity and for understating [40]the entry-deterring effects of output expansions beyond optimal levels, in the range where price falls below marginal cost yet exceeds average cost. Scherer, Predatory Pricing and the Sherman Act: A Comment, 89 Harv. L. Rev. 869 (1976). Scherer's concern is that output and pricing in this range might be used to deter new entry by equally efficient firms when minimum efficient scale is large because residual demand cannot accommodate the additional output required for viable entry. For such a strategy to be effective, of course, the prospective entrant must perceive that the dominant firm is unlikely to make room by reducing its output. Even though actual entry by the new firm would drive prices below the Areeda-Turner levels if the monopolist refused to back off, Scherer believes that the entrant might be unwilling to take the risk that enforcement of the antitrust laws would provide it adequate protection. Scherer at 872.[32]

The scenario sketched by Scherer bears a superficial resemblance to the DuPont situation, inasmuch as it is alleged that DuPont's pricing and growth strategy purposefully served to deter existing firms from developing low-cost ilmenite technology by precluding

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capacity, since they believe that monopolists are unlikely to build costly excess capacity simply to deter new entry and that it would be too difficult to determine whether the excess capacity was attributable to strategic reasons or innocent factors, such as unanticipated changes in demand. Areeda & Turner, Predatory Pricing And Related Practices Under Section 2 of the Sherman Act, 88 Harv. L. Rev. 697, 719 (1975).

[32] In their reply to Professor Scherer, Professors Areeda and Turner express a willingness to modify their standard slightly so that predation could be established if the dominant firm's prices fell substantially below marginal cost, though still above average cost. Areeda & Turner, Scherer on Predatory Pricing: A Reply, 89 Harv. L. Rev. 868, 894 (1976).

them from learning to operate at large, efficient scale. On closer examination, however, the similarity evaporates. Scherer's model assumes that the dominant firm's output is expanded into the range where its average costs are rising and its prices are below marginal cost. But such conduct is not evident here. DuPont does not appear to be operating, or planning to operate, on the upward segment of its average cost curve, either by building a less-than-efficient size plant or by otherwise expanding output beyond optimum levels. Thus, we are unable to find in this part of Scherer's analysis any cause to deem DuPont's expansion and pricing strategy unreasonable.

Of perhaps greater relevance is Scherer's further recommendation that cost-based tests be replaced by a rule-of-reason analysis for gauging the long-run welfare effects of dominant firm behavior. Under such an approach, Scherer suggests that there may be cases where pricing above marginal cost levels should be deemed predatory because of ensuing long-run welfare losses. Of great significance to us, though, is that even here Scherer recognizes the welfare benefits of expansion consistent with optimal scale economies, a situation characteristic of DuPont's expansion program. To Scherer, the proper way to analyze non-traditional forms of dominant firm predation, such as preemptive output expansion, is by an assessment of such variables as

> the relative cost positions of the monopolist and fringe firms, the scale of entry required [41]to secure minimum costs, whether fringe firms are driven out entirely or merely suppressed, whether the monopolist expands its output to replace the output of excluded rivals or restricts supply again when the rivals withdraw, and whether any long-run compensatory expansion by the monopolist entails investment in scale economy-embodying new plant. Scherer, at 890.

Since DuPont, the low-cost producer, is not seeking to displace existing output,[33] or to increase output temporarily to head off competitive expansion, it seems difficult to condemn its expansion efforts, which are directed at capturing future growth in demand. Of course, it can be argued that other TiO_2 producers would eventually achieve cost parity with DuPont (estimated ten years) if they were encouraged to expand to large scale operations. But it seems anomalous to preclude DuPont from competing for this increased demand on grounds that it could do so most efficiently only at a level

[33] DuPont's plan, if successful, will, of course, reduce the market share of rivals over time, but that is still considerably different from a program designed simply to substitute DuPont's output for that of its competitors. It should also be repeated that DuPont's increase in market share since 1972 has come largely at the expense of competitors, including imports, due to two factors—increased capacity provided by expansion of DuPont's existing facilities and a leveling off of demand after 1972. These market share inroads, of course, are attributable to unexpected changes in market conditions.

of capacity and output that inevitably tends to exclude other competitors.

Professor Williamson also emphasizes the strategic aspects of predatory pricing, but he focuses on a somewhat different problem. Williamson, Predatory Pricing: A Strategic and Welfare Analysis, 87 Yale L. J. 284 (1977). Specifically, Williamson assumes that dominant firms will respond to cost-based predatory pricing rules, such as the Areeda-Turner test, by deliberately choosing a pre-entry plant scale that enables them to meet new entry by expanding output to levels that remain profitable for them but not for their putative rivals. In short, by building in excess capacity, the established firm can turn back new entry without violating the applicable cost-based pricing standard. Under this scenario, potential entrants are presumed to have access to the same cost-saving technology as the dominant firm, although cost parity may be achieved only with operational experience.

The cornerstone of Williamson's solution to this problem is his output restraint rule, which precludes dominant firms (60% market share) from disproportionately expanding output (above their historical shares of demand) in response to new entry. [42]Such a rule, presumably, would force large firms anticipating entry to set their pre-entry output at higher levels, thereby leading to a more efficient utilization of resources.[34]

On its face, the kind of preemptive expansion addressed by Williamson differs from the DuPont facts. Williamson's concern seems to be with short-term strategic responses by dominant firms that are designed primarily to discipline the behavior of rivals rather than to take advantage of efficiencies in serving long-term demand growth. By contrast, in this matter, we cannot find that DuPont's plan was designed simply or even primarily for the purpose of blocking expansion moves of competitors (although that certainly may have been an effect). Moreover, with respect to Williamson's additional rule for pricing by established firms, which is keyed to full cost recovery, it appears evident that DuPont's pricing also met this standard, there being no suggestion by complaint counsel that DuPont's prices either in the short run or the long run failed to cover costs plus a reasonable return on investment.

Complaint counsel also refer us to an article by Professor Spence for the proposition that investment in new capacity may be a more

[34] This approach has been criticized by Professor Schmalensee for being difficult to apply and for not adequately addressing all forms of predation. Schmalensee generally prefers the Scherer approach, although he suggests that an average cost test may be a more workable standard for judicial application in predatory pricing cases. Schmalensee, On the Use of Economic Models in Antitrust: The ReaLemon Case, 127 Pa. L. Rev. 994, 1029 (1979).

effective entry-deterring device than price cutting. Spence, Entry Capacity, Investment and Oligopolistic Pricing, 8 Bell J. of Econ. 534 (1977). Spence contends that capacity expansion may be used strategically to deter entry, but his concern is with practices quite different from those in the present case.

> The principle of this [Spence] model is quite simple. It is that existing firms choose capacity in a strategic way designed to discourage entry. *This strategic purpose is realized by holding excess capacity in the preentry period.* This excess capacity permits existing firms to expand output and reduce price when entry is threatened, thereby reducing the prospective profits of the new entrant who operates on the residual demand curve to zero. (emphasis added). Id. at 534-35. [43]

While Spence's model really addresses excess capacity carried by an entire industry, rather than a single firm, we recognize its potential applicability to single-firm behavior; even so, we distinguish the conduct of DuPont. It cannot be said that DuPont built excess capacity to hold in reserve as a means of disciplining existing rivals or deterring new entry. DuPont's original plan conformed to demand estimates, and there is no persuasive evidence that DuPont unreasonably refused to delay or cancel De Lisle in the face of declining demand simply as a way to keep competitors in check. Also, the fact that there is capability for a second new line at De Lisle does not lead us to conclude that DuPont artificially or unreasonably attempted to head off competitive expansion in the context of the Spence model.

In a more recent article, Professors Joskow and Klevorick pull together some of the theories and concepts previously discussed and advance a two-tiered approach to dealing with predatory pricing. Joskow & Klevorick, A Framework for Analyzing Predatory Pricing Policy, 89 Yale L. J. 213 (1979). They propose that structural conditions determine whether the market is conducive to predation; if it is, a set of behavioral rules would be applied to gauge the legality of the dominant firm's pricing practices. Under their approach, monopoly pricing that fails to cover average total costs would be presumed to be predatory, except in limited circumstances, for example, where excess capacity is attributable to a declining industry.[35]

As for pricing above average costs, Joskow and Klevorick believe that in certain circumstances temporary price cuts by dominant firms to levels above average cost may also be predatory. They propose the following rule:

> A price decrease to a point above average total cost would be presumed to be legal

[35] Professor Posner also advocates an average cost test as the proper basis for assessing the legality of monopoly pricing. R. Posner, Antitrust Law: An Economic Perspective 184-96 (1976).

unless the price cuts were reversed either fully or to a significant extent within a reasonable period of time—for example, two years. *Id.* at 255.

Under this rule, any reversal in price would have to be justified by changes in demand or costs, and the predatory pricing would have to "run its course" before relief would be available.[36] [44]

Comparing DuPont's strategy with the Joskow & Klevorick approach reveals some obvious distinctions. For one thing, it is not clear whether DuPont, in 1972 or even today, enjoys the kind of entrenched monopoly power that Joskow & Klevorick view as a critical prerequisite to the application of their behavioral standards, although there is evidence that DuPont has some degree of market power. More importantly, as noted elsewhere, there is no allegation of below-cost pricing here, whether the standard is average variable or average total costs. To be sure, these authors offer a separate non-cost standard that looks to temporary price deviations and the circumstances surrounding those deviations, but implicit in their model is a concern for short-run responses to competitive inroads that are divorced from such market factors as new growth opportunities or superior technology.[37] When coupled with the demand projections and cost advantages extant here, the DuPont strategy reveals long-term considerations that are of a character considerably different from the short-run price cutting addressed by Joskow & Klevorick.

To summarize, the focus of much of the literature centers on strategic responses to new entry, or, as characterized by Williamson, responses "of a gaming variety—now it's there, now it isn't, depending on whether an entrant has appeared or perished. . . ." Williamson, 87 Yale L. J. at 339. Such behavior hardly typifies DuPont's expansion plan, which contemplated a permanent increase in plant capacity and output. Even as to respondent's pricing objectives—generating funds for its own expansion while [45]discouraging similar efforts by competitors—those objectives were

[36] Another commentator, Professor Baumol, advocates a predatory pricing rule that precludes monopolists from rescinding price cuts made in response to the threat of entry for a reasonable period of time. Baumol, n. 20 *supra.*

[37] While the authors downplay the significance of evidence concerning subjective intent, they believe it may be of some value where the evidence clearly indicates (1) that the monopolist plans to increase prices after driving competition from the market, and (2) the price cuts are being used "to increase artificially the difficulty of entering the market." What they mean by this is evidence of long-range plans by a monopolist to preserve its market power through erection of entry barriers or outright elimination of competing firms. In this connection, the authors observe that allegations of predatory pricing are often accompanied by charges that firms have engaged in other non-price forms of predation, such as " 'targeted' advertising expenditures, 'false' product announcements and product 'manipulations.' " Joskow & Klevorick, A Framework For Analyzing Predatory Pricing Policy, 89 Yale L. J. 213, 259, n. 92 (1979). But they acknowledge that the issues may not be resolved easily because of the difficulty of distinguishing artificial exclusionary behavior from legitimate responses to competition. Similar issues are involved here inasmuch as DuPont is charged with having developed a predatory scheme that involves interrelated pricing, expansion and announcement practices.

consistent with DuPont's cost advantage and undertaken in conjunction with the firm's long-term growth in response to demand projections; they were not undertaken simply as a device to retard entry without regard to independent market forces.

To be sure, the recent literature does not fully address all forms of exclusionary conduct, especially where the actions are of a longer-term nature. To the extent that it does we can find no persuasive basis for declaring DuPont's behavior unlawful. The conduct at issue here, for example, does not appear to be the kind of artificial, entry-barrier raising behavior cited by Professors Joskow & Klevorick. *See* n. 37 *supra.* DuPont's actions may make future competitive expansion more difficult, but that effect is not the product of artificially induced conduct that is unrelated to market conditions, cost differences or scale economies.

Thus, although the literature to date on the subject of predation is not exhaustive, nor has it produced a consensus among the commentators, it does provide a valuable framework for looking at the merits of this case. As such, we find no compelling basis in the various analyses for judging DuPont's behavior to be unreasonable.

c) *Conclusions*

Having reviewed the legal precedents and economic literature on the subject of predation, we believe that the conduct under question should be assessed generally in light of the respondent's market power, the nature of its conduct and prevailing market conditions. As the firm's market power approaches monopoly proportions, the standard for measuring the legality of the firm's behavior would more closely approximate the standard applicable to monopolists.

We recognize, of course, the importance of providing as much guidance to business as possible, so that desirable competitive behavior is not chilled, even by a firm with considerable market power. Nevertheless, some uncertainty in dealing with dynamic market factors is probably unavoidable. No one simple test seems adequate. We suspect, however, that in many instances the challenged conduct can be fairly categorized as clearly legitimate competitive behavior, on the one hand, or as behavior which clearly has little or no redeeming justification, on the other hand. For the gray areas in between, we believe there is no substitute for a careful, considered look at the overall competitive effects of the practices [46] under scrutiny.[38] In the absence of a stronger consensus among the

[38] At a more specific level, some of the factors that appear especially pertinent to a proper rule-of-reason type analysis include: (1) the extent to which the conduct enhances efficiency or innovation, including profitability considerations; (2) the extent to which the conduct is a reaction to competitive behavior, demand shifts, new

(Continued)

courts and commentators as to the lawful parameters of monopoly or dominant firm behavior, we believe that a balancing approach, which takes due account of rational, efficiency related conduct, is best suited to the task at hand.[39]

Recalling Judge Wyzanski's comments in *United Shoe Machinery,* he observed that the practices at issue there involved

> contracts, arrangements, and policies which instead of encouraging competition based on pure merit, further the dominance of a particular firm. In this sense, they are *unnatural* barriers; they *unnecessarily* exclude actual and potential competition; they restrict a free market. 110 F. Supp. at 344-45 (emphasis added). [47]

This characterization, though addressing monopoly behavior, effectively summarizes the kind of approach that remains relevant today for dealing with market power-related conduct. Similar considerations are reflected in the decisions in *Greyhound,* 559 F.2d at 498 (whether practices "unnecessarily excluded competition") and *Transamerica,* 481 F. Supp. at 1022 (conduct proscribed which "unreasonably restrict[s] competition").

In applying these principles to the facts of this case, it is useful to restate complaint counsel's fundamental objection to DuPont's growth plan. In essence, complaint counsel contend that it was logical for DuPont to do what it did only if monopoly power could be attained in the future. It is argued that DuPont's construction/pricing/non-licensing policy involved a current foregoing of available profits, that DuPont recognized that it could recoup those profits down the road through high volume and higher prices, and that DuPont's policy only made sense if those excess profits would become available at a later date.

Put differently, DuPont presumably would not have tried to capture all future demand growth, and thereby risked the costs of operating a plant the size of DeLisle at less than capacity, unless it was reasonably assured that other competitors could not expand. DuPont obtained this assurance, it is claimed, not through normal market forces, but rather through its own efforts, as evidenced by the combination of expansion, announcement, pricing and licensing

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technology or other market conditions; (3) the permanence or reversibility of the challenged actions; (4) the alternatives available to the firm; and (5) the effect of the conduct on entry barriers and rival firm behavior. As we have noted, however, resort to such benchmarks as whether the practices constituted "ordinary" or "typical" business behavior may be of some value, but they can hardly be expected to serve as reliable indicators of competitive effects, especially where market power is substantial and entry barriers high. Even behavior that improves efficiency or technology may still be unreasonable, since the benefits may be only incidental in relation to the adverse effects (*e.g.*, improvements instituted merely as a temporary measure for the purpose of driving competitors out of the market). As we have seen, increases in output, a normal and usually legitimate form of competitive behavior, may be used primarily as an exclusionary tactic.

[39] Professor Cooper also provides some helpful considerations for determining the reasonableness of behavior in attempt cases, Cooper, Attempts and Monopolization; A Mildly Expansionary Answer to the Prophylactic Riddle of Section Two, 72 Mich. L. Rev. 373, 449 (1974).

policies. As further proof of the overall strategy, complaint counsel cite to DuPont's pricing forecasts, which it is argued clearly reveal respondent's plan to sacrifice short-term profits for long-term monopoly gains.

We simply cannot accept this analysis. The rationality of DuPont's program hardly seems dependent on its ability to extract monopoly profits in the future. DuPont had a highly efficient process, indeed the most efficient in the industry, and it anticipated expanding market demand. To serve that demand, DuPont enlarged its existing facilities to optimal levels and built a new plant of efficient scale (but not above efficient levels and no larger than necessary to satisfy predicted demand) to serve the market it expected would develop. Given respondent's level of efficiency, expansion of the magnitude undertaken would make sense, regardless of whether the firm would eventually be able to raise prices above competitive levels. Moreover, DuPont's pricing policies were entirely consistent with its cost advantage and apparently (for there is no suggestion that it engaged in predatory pricing) were profitable, even during the '70s when respondent was arguably foregoing additional profits. [48]

Even if DuPont could earn future profits equal to those it was passing up in the mid-1970s only if existing competitors were dissuaded from expanding, it does not necessarily follow that actions leading to that result should constitute an illegal attempt to monopolize. As we have observed, DuPont's ability to pursue its strategy derived from substantial economic efficiencies; it did not stem from below cost pricing, false plant announcements, construction of excess capacity or other plainly anticompetitive conduct. Complaint counsel contend, however, that notwithstanding these efficiencies and DuPont's conceded right to expand, there were less restrictive alternatives available that would have less adverse competitive consequences. In particular, they cite DuPont's own more moderate expansion program—a program discarded in favor of the more aggressive growth plan in 1972—which contemplated only expansion of existing plants. More generally, complaint counsel and their expert witness, Professor Shepherd, urged that DuPont should have pursued *any* less aggressive strategy than the one it did. In other words, respondent should not have attempted to capture all the growth in the market, thereby making it more difficult for competitors to expand to the scale justified by DuPont's technology.

While it is proper and desirable to consider alternative courses of conduct open to DuPont, we firmly believe the course chosen was not unreasonable. When DuPont conceived its strategy in 1972, its estimates of demand growth and supply shortfall seemed reasonable,

and there has been no suggestion to the contrary. In competing for this growth, DuPont realized that even expansion of its existing plants to their practical limits could not satisfy all of the additional demand expected through the early 1980s. A new plant would be required. To build such a plant at efficient scale, afforded by DuPont's developed technology, meant that there would be little, if any, room left for expansion by competitors. Yet, to deny DuPont the opportunity to compete for all of the projected demand growth unduly penalizes its technological success. To require respondent to build a smaller, less efficient plant, or no plant, under these circumstances would be an unjustified restraint on competitive incentives and an unjustified denial of the benefits of competition to consumers.

To be sure, DuPont had another alternative. It could have licensed its technology to competitors, as suggested by complaint counsel, thereby enabling respondent's rivals to close the technological gap more quickly. But, in the context of this case, we can find no basis for concluding that DuPont's refusal to license its technology, whether taken separately or together with the other conduct, was unjustified. There is no evidence, for example, that respondent used unreasonable means to acquire its know-how, or that it joined with others in preventing access by competitors. Complaint counsel cite no authority for the proposition that DuPont should have [49]licensed its technology, and we are aware of none.[40] Whatever may be the proper result in other factual settings, we are not persuaded that the refusal to license in this situation provides a basis for liability; in fact, imposition of a duty to license might serve to chill the very kind of innovative process that led to DuPont's cost advantage.

Turning to the pricing options available to respondent, there is, of course, no evidence that DuPont priced below its costs, since the case was not tried on such a theory. As for the issue of limit pricing, the literature discussed previously suggests that predation may occur even in circumstances where prices are above the dominant firm's costs (whether measured by average variable or average total cost). In this respect, it seems clear that respondent sought to price in a fashion that took account of the propensities and abilities of

[40] To the contrary, the recent *Berkey* and *IBM* cases suggest that firms (monopolists and non-monopolists) that have achieved success through superior products and business acumen, and not unlawful anticompetitive conduct, are under no duty to license or disclose their technology to their rivals. *Berkey Photo, Inc.* v. *Eastman Kodak Co.*, 603 F.2d 263 (2d Cir. 1979); *California Computer Products, Inc.* v. *IBM Corp.*, 613 F.2d 727 (9th Cir. 1979); *Transamerica Computer Co.* v. *IBM Corp.*, 481 F. Supp. 965 (N.D. Cal. 1979); *ILC Peripherals Leasing Corp.* v. *IBM Corp.*, 458 F. Supp. 423 (N.D. Cal. 1978). Here, DuPont's refusal to license its technology is not a factor that would make otherwise reasonable behavior unreasonably anticompetitive. And, if the other conduct were itself unreasonable, the refusal to license would add little to the case, except, of course, as a possible basis for remedial action. See also *SCM Corp.* v. *Xerox Corp.*, 463 F. Supp. 983 (D. Conn. 1978).

competitors to expand, although the firm's pricing decisions were affected at least in part by independent economic forces, such as demand conditions. Given this situation, it can be argued that these pricing policies went too far, that they transformed an otherwise legitimate method of expansion into an unlawful course of conduct.

We do not agree. DuPont's pricing strategy stemmed from its clear cost advantage over competitors and occurred in conjunction with its long-term plan to capture future market growth, a plan which we have pointed out before was consistent with foreseeable demand and scale economies. Thus, this is not a case where DuPont was attempting solely to preserve its market power through selective, temporary price cuts to deter new entry or expansion by existing competitors. Even complaint counsel do not attack respondent's pricing as an independent violation; rather they argue that it is unlawful as part of a broader pattern of behavior. For our part, even if DuPont's pricing can be characterized as a form of limit pricing, we do not find it to be unreasonable, absent at least some evidence of below-cost pricing, [50]in view of the firm's cost advantage, its market position and its legitimate expansion efforts. While there may be circumstances where above cost pricing is unjustifiably exclusionary, those circumstances clearly are not present here.

We also do not find that DuPont's announcements of its early plans to build an unidentified additional facility or its later announcements identifying the De Lisle plant were unfairly exaggerated or misleading threats or signals in the strategic sense suggested by the commentators. Because of the lead time required for obtaining environmental permits and for completing construction, DuPont's early disclosure of its plans appears logical. The documents also reflect DuPont's strong belief that unfavorable customer reaction could be expected if it cancelled or postponed De Lisle for any significant length of time, so that there were disincentives to making false or exaggerated announcements. Had these announcements been false or grossly disproportionate, under circumstances suggesting they served little purpose except to mislead and discourage competition, there might have been a basis for liability. *Cf. Bergjans Farms Dairy Co.* But that is not the case before us. Moreover, DuPont's decisions to scale back the size of De Lisle and delay its start-up are attributable, in large measure, to unforeseen changes in supply and demand and therefore do not render the otherwise justified announcements unreasonable.

As an additional argument, complaint counsel contend that DuPont's cost advantage is largely fortuitous, owing to technology developed many years before. Without expressly suggesting that the

result should be different had DuPont developed the ilmenite process in 1972, complaint counsel nevertheless argue that DuPont's allegedly superior skills and business acumen should be given little weight. More specifically, they contend that DuPont had demonstrated no contemporaneous technological superiority because it has not "*recently* distinguished itself as an organizational innovator," citing Williamson, *Dominant Firms and the Monopoly Problem: Market Failure Considerations,* 85 Harv. L. Rev. 1512, 1527 (1972) (emphasis in original). But the point of Williamson's discussion is whether an established monopolist should be able to defend against a charge of monopolization on traditional grounds of business acumen or historic accident, where such causes bear little relationship to the reasons for the firm's continuing dominance. The issues here are considerably different.

We believe it would be anomalous to downgrade the significance of DuPont's technological superiority simply because the fruits were not reaped simultaneously with the discovery of the process. It may well be that DuPont anticipated possible future shortages of rutile and other ores back in the '40s and '50s, even though it could not have anticipated precisely the events that occurred in the late '60s. In any event, DuPont's development of an alternative supply source reflects the kind of skill and foresight that should be encouraged, whether the benefits materialize immediately or at some later date. [51]

With the possible exception of *Alcoa,* which involved repeated increases in output by a monopolist, there is nothing in the case precedents to suggest that DuPont's expansion program unnecessarily heightened entry barriers or otherwise unreasonably excluded competition. Nor does the conduct appear to be sufficiently similar to the preemptive kinds of expansion described by Professors Scherer and Williamson to warrant condemnation. To the extent that the effects of DuPont's expansion bear any resemblance to those models, a review of factors such as those suggested by Scherer's rule-of-reason approach would still call for a finding of reasonableness.[41]

It may be that DuPont ultimately will achieve a monopoly share of the market. As its share increases, other firms may find it harder to capture the efficiencies enjoyed by DuPont due to the scale economies associated with the ilmenite process. Those effects should be weighed carefully, and we have done so. Antitrust policy wisely disfavors monopoly, but it also seeks to promote vigorous competitive behavior. Indeed, the essence of the competitive process is to induce

[41] See discussion of Scherer's criteria at pp. 40–41, *supra.*

firms to become more efficient and to pass the benefits of the efficiency along to consumers. That process would be ill-served by using antitrust to block hard, aggressive competition that is solidly based on efficiencies and growth opportunities, even if monopoly is a possible result. Such a view, we believe, is entirely consistent with the "superior skill, foresight and industry" exception in *Alcoa* and subsequent cases, for those decisions clearly indicate that monopolies may be lawfully created by superior competitive ability.[42]

As we have previously indicated, DuPont engaged in conduct consistent with its own technological capacity and market opportunities. It did not attempt to build excess capacity or to expand temporarily as a means of deterring entry. Nor did respondent engage in other conduct that might tip the scales in the direction of liability, such as pricing below cost, making false announcements about future expansion plans, or attempting to lock up customers in requirements contracts to assure the success of its growth plans. In short, we find DuPont's conduct to be reasonable. Accordingly, we affirm the ALJ's dismissal of the complaint.

Final Order

This matter has been heard by the Commission upon the appeal of complaint counsel from the initial decision and upon briefs and oral argument in support of and in opposition to the appeal. For the reasons stated in the accompanying Opinion, the Commission has determined to sustain the initial decision. Complaint counsel's appeal is denied. Accordingly,

It is ordered, That the complaint is dismissed.

[42] If a monopoly results that proves impervious to competitive inroads and is unjustified by scale economies or other efficiencies, antitrust action in this or some other forum may be warranted, even in the absence of abusive conduct. See note 23 *supra;* see also Statement of the Federal Trade Commission to the National Commission for the Review of Antitrust Laws and Procedures (Nov. 17, 1978), Report to the President and the Attorney General, 407. That, however, is an issue entirely different from the one before us.

IN THE MATTER OF

SKF INDUSTRIES, INC., ET AL.

MODIFIED ORDER IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket 9046. Decision, July 5, 1979—Modified Order, October 21, 1980

In accordance with the settlement agreement reached by respondents and Commission counsel without adjudication, and filed with the Court of Appeals for the Second Circuit on July 23, 1980, this modified order revises the "final order" issued by the Commission on July 5, 1979 (44 FR 47926, 94 F.T.C. 6), by changing, among other things, the amount of TRB that SKF may sell to Federal Mogul and the requirements for publishing the provisions of the order.

MODIFIED ORDER TO CEASE AND DESIST

Respondents SKF Industries, Inc. ("SKF"), and Federal-Mogul Corporation ("FM") having filed in the United States Court of Appeals for the Second Circuit petitions for review of the Commission's "Final Order" herein dated July 5, 1979; and a stipulation dated July 23, 1980, by and among SKF, FM and counsel for the Commission having been entered into and filed with the Court of Appeals, pursuant to which the parties agreed and consented to entry by the Court of Appeals, without adjudication of any issue of law or fact, of an order modifying said "Final Order" in accordance with said stipulation and directing that said "Final Order," as so modified, be enforced; and the Court of Appeals having thereupon entered an Order, dated August 25, 1980, remanding the proceeding to the Commission with directions to modify said "Final Order" in accordance with said stipulation:

Now, therefore, it is hereby ordered, That the aforesaid "Final Order" be, and hereby is, modified in accordance with the order of the Court of Appeals to read as follows:

FINAL ORDER

I

This Order shall be deemed to be final as of December 31, 1979, and be binding on Federal-Mogul Corporation ("FM"), SKF Industries, Inc. ("SKF"), their subsidiaries or any person under the control of FM or SKF, their successors and assigns, and their officers, agents, representatives and employees.

II

It is ordered, That the agreement signed by SKF and FM on December 17, 1974, and any similar arrangements between or among respondents, including the understandings reflected in the exchange of documents on January 27, 1972, shall be cancelled as of the date as of which this Order becomes final.

III

It is ordered, That, for purposes of this Order, the following definitions shall be applicable:

(i) *0″–4″ TRB*—tapered roller bearings having an outside diameter of zero to four inches.

(ii) *Automotive Aftermarket*—the domestic replacement market, including all intermediate suppliers to such market (but excluding FM and the manufacturers of original equipment who purchase 0″–4″ TRB for distribution to service customers through their dealers and franchisees), for 0″–4″ TRB for use in passenger cars, light and heavy trucks, buses, trailers, tractors, self-propelled agricultural equipment and vehicles, such as trailers, and agricultural equipment pulled by self-propelled vehicles.

(iii) *FM TRB Requirements*—the total dollar value of purchases of 0″–4″ TRB by FM from all sources (including sources owned or controlled by FM) for distribution in the United States. The value of purchases of 0″–4″ TRB by FM from sources which it owns or controls shall be either cost to FM or the fair market value, whichever is less.

(iv) *FM TRB Purchases from SKF*—the total dollar value of direct or indirect purchases by FM of 0″–4″ TRB from SKF, Aktiebolaget SKF ("AB SKF"), or any person under the control of SKF or AB SKF for distribution in the United States, which shall include (A) purchases by FM or 0″–4″ TRB manufactured by SKF, AB SKF, or any person under the control of SKF or AB SKF, and (B) purchases by FM under the arrangement to which SKF, AB SKF, or any person under the control of SKF or AB SKF is a party or from a supplier in which SKF, AB SKF, or any person under the control of SKF or AB SKF has an interest.

(v) *TRB Units*—0″–4″ TRB as purchased by Automotive Aftermarket customers of SKF. Purchases may be (i) an assembled TRB, (ii) a TRB outer ring (cup), or (iii) a TRB inner ring (cone), each being a single TRB unit.

(vi) *SKF Net Aggregate Sales to the Automotive Aftermarket*—that

number of TRB Units which is the difference between (i) the aggregate number of TRB Units sold by SKF to the Automotive Aftermarket and (ii) the number of TRB Units, if any, which must be subtracted therefrom so that of the resulting number of TRB Units sold by SKF to the Automotive Aftermarket no more than 15% represents TRB Units sold by SKF to or through any national organization of independent warehouse distributors by or through which, as of the effective date of this Order, all the members of such organization secure all of their needs of 0″–4″ TRB from the same single source, other than SKF.

IV

With respect to FM TRB Purchases from SKF, *it is ordered,* That the following limitations shall apply during the periods described below:

(i) The time period covered by any given purchase order or related agreement concerning FM TRB Purchases from SKF shall not exceed twelve (12) months.

(ii) The aggregate dollar value of any FM TRB Purchases from SKF during the first thirty-six (36) month period following the date as of which this Order becomes final (calendar years 1980, 1981 and 1982) shall not exceed 60% of the FM TRB Requirements during that period. The allowable percentage under this subparagraph shall include any 0″–4″ TRB purchased, but not sold, by FM from SKF, AB SKF, or any person under the control of SKF or AB SKF prior to the date as of which this Order becomes final.

(iii) The aggregate dollar value of any FM TRB Purchases from SKF during the second thirty-six (36) month period following the date as of which this Order becomes final (calendar years 1983, 1984 and 1985) shall not exceed 50% of the aggregate FM TRB Requirements during that period.

(iv) The aggregate dollar value of any FM TRB Purchases from SKF during the third thirty-six (36) month period following the date as of which this Order becomes final (calendar years 1986, 1987 and 1988) shall not exceed 40% of the aggregate FM TRB Requirements during that period; *provided, however,* that if the SKF Net Aggregate Sales to the Automotive Aftermarket shall have been 1,250,000 or more TRB units during the second thirty-six (36) month period following the date as of which this Order becomes final (calendar years 1983, 1984 and 1985), the aggregate value of any FM TRB Purchases from SKF shall not exceed 50% of the aggregate FM TRB

Requirements during the third thirty-six (36) month period (calendar years 1986, 1987 and 1988).

(v) The aggregate dollar value of any FM TRB Purchases from SKF during the fourth thirty-six (36) month period following the date as of which this Order becomes final (calendar years 1989, 1990 and 1991) shall not exceed 40% of the aggregate FM TRB Requirements during that period; *provided, however,* that if the SKF Net Aggregate Sales to the Automotive Aftermarket shall have been 1,250,000 or more TRB Units during the third thirty-six (36) month period following the date as of which this Order becomes final (calendar years 1986, 1987 and 1988), the aggregate value of any FM TRB Purchases from SKF shall not exceed 50% of the aggregate FM TRB Requirements during the fourth thirty-six (36) month period (calendar years 1989, 1990 and 1991).

(vi) This Order shall automatically terminate as of December 31, 1991.

V

It is further ordered, That each respondent shall notify all persons having sales and policy responsibilities in its organization of the terms of this Order, and respondents together shall publish same in a major trade journal or periodical within six months following the conclusion of the first twelve (12) month period (calendar year 1980) and again within six months following the conclusion of the second twelve (12) month period (calendar year 1981) following the date as of which this Order becomes final; *provided, however,* that if during either such twelve (12) month period (calendar year 1980 or 1981) the aggregate dollar value of any FM TRB Purchases from SKF shall not have exceeded 50% of the aggregate FM TRB Requirements during that period, then such publication following the conclusion of that period may be omitted.

VI

It is further ordered, That each respondent shall notify the Commission at least thirty (30) days prior to any proposed change in said respondent which may affect compliance obligations arising out of this Order, such as dissolution, assignment or sale resulting in the emergence of a successor corporation, or the creation or dissolution of subsidiaries or joint ventures.

VII

It is further ordered, That within sixty (60) days after the date of issuance of this Order, and within sixty (60) days after the end of each calendar year during which this Order is effective, each respondent shall file with the Federal Trade Commission a written report setting forth in detail the manner and form of its compliance with this Order.

VIII

It is further ordered, That after the end of calendar year 1984, after the end of each quarter during calendar year 1985, and after the end of calendar year 1985, respondent SKF shall report to the Commission the SKF Net Aggregate Sales to the Automotive Aftermarket during the period beginning January 1, 1983, to and including the effective date of the report. These reports shall be filed within forty-five (45) days after the end of the respective reporting periods and shall be made available to respondent FM at the time they are filed with the Commission. This reporting obligation shall automatically terminate upon the filing by SKF of such a report indicating that the SKF Net Aggregate Sales to the Automotive Aftermarket have equalled or exceeded 1,250,000 TRB Units during such period.

IX

It is further ordered, That after the end of calendar year 1987, after the end of each quarter during calendar year 1988, and after the end of calendar year 1988, respondent SKF shall report to the Commission the SKF Net Aggregate Sales to the Automotive Aftermarket during the period beginning January 1, 1986, to and including the effective date of the report. These reports shall be filed within forty-five (45) days after the end of the respective reporting periods and shall be made available to respondent FM at the time they are filed with the Commission. This reporting obligation shall automatically terminate upon the filing by SKF of such a report indicating that the SKF Net Aggregate Sales to the Automotive Aftermarket have equalled or exceeded 1,250,000 TRB Units during such period.

IN THE MATTER OF

THE MENTHOLATUM COMPANY, INC.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF SECS. 5 AND 12 OF THE FEDERAL TRADE COMMISSION ACT

Docket C-3047. Complaint, Oct. 22, 1980—Decision, Oct. 22, 1980

This consent order requires, among other things, a Buffalo, N.Y. producer of denture cushions to use advertisements which are consistent with labeling information included with the product concerning health, safety or efficacy; to disclose, in those instances where the firm makes claims of duration of use, such labeling warnings in a clear and conspicuous manner; and, further, to affirmatively state that its product is intended for short-term use only.

Appearances

For the Commission: *Leslie Fax.*

For the respondent: *Samuel Magavern, Magavern, Magavern, Lowe, Beilewech, Dompkins & Fadale,* Buffalo, N.Y.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that The Mentholatum Company ("Mentholatum"), a corporation, hereinafter referred to as respondent, has violated the provisions of the Federal Trade Commission Act, and that a proceeding with respect to such violations would be in the public interest, hereby issues its complaint, setting forth its charges as follows:

PARAGRAPH 1. Mentholatum is a corporation organized, existing, and doing business under and by virtue of the laws of the State of Delaware, with its principal office and place of business located at 1360 Niagara St. in the city of Buffalo, New York.

PAR. 2. Respondent Mentholatum is now, and for some time last past has been engaged in the production, advertising, offering for sale, sale and distribution of denture cushions designated by the trade name "Snug Denture Cushions." This product, as advertised, is a "device" within the meaning of Section 12 of the Federal Trade Commission Act, 15 U.S.C. 52.

PAR. 3. In the course and conduct of its business, respondent Mentholatum causes and has caused the said products, when sold, to be transported from its place of business in one State of the United

States to purchasers thereof located in various other States of the United States and the District of Columbia. Respondent Mentholatum maintains, and at all times mentioned herein has maintained, a substantial course of trade in Snug Denture Cushions in or affecting commerce.

PAR. 4. In the course and conduct of its business, respondent has disseminated or caused the dissemination of various advertisements for Snug Denture Cushions across state lines by various means in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, including advertisements inserted in magazines and newspapers and also advertisements broadcast on national television networks. The purpose of all these advertisements has been to induce, directly or indirectly, the purchase of Snug Denture Cushions, and it is likely that these advertisements have succeeded in inducing consumers to purchase this product.

PAR. 5. Typical, but not all inclusive, of the statements and representations in said advertisements are those found in Exhibits A–G attached to this complaint, including such representations as the following:

a. Newspaper and magazine advertisements:

(1) ELIMINATES DAILY DENTURE "FIXINGS" FOREVER— Snug Cushions hold dentures comfortably tight for weeks.

(2) HOLDS DENTURES FIRM WITHOUT DAILY "FIXINGS"—Snug Cushions hold dentures comfortably tight for weeks.

(3) NEW FREEDOM FROM DAILY DENTURE "FIXINGS"—Snug Cushions hold dentures comfortably tight for weeks.

b. Television Advertisements:

(1) Sara: Didn't I tell you about Snug? It's different—you don't need to apply it every day . . . Snug lasts for weeks. And it'll hold your dentures firm and comfortable.

. . . [At a point later in time]

Sara: Didn't you switch to Snug

Helen: Sure . . .

(2) Thousands of denture wearers have long suffered with loose, wobbly, uncomfortable plates. Now many use Snug Brand Denture Cushions . . . .

PAR. 6. Through the use of said advertisements and others similar thereto not specifically set out herein, disseminated as aforesaid, respondent has made or is making the following representations:

(a) that Snug Denture Cushions are appropriate for long-term use;

(b) that Snug Denture Cushions are for use other than temporary use only until a dentist can be seen.

PAR. 7. In fact, the labeling on Snug Cushions states:

(a) On the package:

Caution: Long term use of an ill-fitting denture, reliner, pad or cushion may lead to swelling, faster bone resorption, or continuing irritation. Use Snug temporarily until you can see your dentist.

(b) On the package insert:

(1) Snug Denture Cushions are for *temporary* use only . . .

(2) Dentures that do not fit properly cause irritation and injury to the gums and faster bone loss which is permanent and may require a completely new denture. Changes in the gums caused by dentures that do not fit properly may require surgery for correction. Continuing irritation and injury may lead to tumors in the mouth. Use of denture reliners, pads, and cushions may temporarily decrease the discomfort. However, their use will not make the denture fit properly. Special training and tools are needed to fit properly. You must see your dentist for a new denture or a repair as soon as possible.

PAR. 8. The representations referred to in Paragraph Six are inconsistent with, negate, and contradict the labeling on respondent's product as set forth in Paragraph Seven hereof. Such inconsistency, negation, and contradiction has the tendency and capacity to mislead and deceive purchasers of said product as to its proper duration of use, and to negate the import and purposes of and to detract from the effectiveness of the warnings, cautions, limitations and instructions for use found in the labeling.

Therefore, the advertisements, acts and practices, referred to in Paragraph Six above were and are unfair and deceptive.

PAR. 9. Furthermore, in its advertising for Snug Denture Cushions, respondent has been and now is making claims as to the duration of use of said product without clearly and conspicuously disclosing to the purchasing public that the labeling for Snug Denture Cushions states that said product should be used only on a temporary basis until a dentist can be seen.

PAR. 10. The existence and substance of the above-mentioned labeling warning is a material fact in light of the representations set forth in Paragraphs Five and Six regarding duration of use, in that disclosure of the warning to consumers would be likely to affect their decisions of whether or not to purchase said product and of how properly to use it. Respondent's failure to disclose this material fact has the tendency and capacity to mislead and deceive consumers into the mistaken belief that no such warning exists.

Therefore, the advertisements, acts and practices referred to in Paragraphs Five and Six above were and are false, deceptive, and unfair.

PAR. 11. In the course and conduct of its business as aforesaid, and

at all times mentioned herein, respondent Mentholatum has been in substantial competition in commerce, with corporations, firms and individuals in the sale of products of the same general kind and nature as those advertised and/or sold by respondent.

PAR. 12. The aforesaid unfair and deceptive acts and practices of respondent have had and now have, the capacity to induce members of the purchasing public to purchase substantial quantities of said product.

PAR. 13. The aforesaid acts and practices of respondent, as herein alleged, were and are all to the prejudice and injury of the public and of respondent's competitors and constituted and now constitute, unfair and deceptive acts and practices and unfair methods of competition in or affecting commerce, in violation of Sections 5 and 12 of the Federal Trade Commission Act. The acts and practices of respondent, as herein alleged, are continuing and will continue in the absence of the relief herein requested.

SNUG DENTURE CUSHIONS

SEE INSTRUCTIONS INSIDE

SNUG DENTURE CUSHIONS

SNUG®

BRAND

DENTURE CUSHIONS

For Upper or Lower Plates

Ever-soft Plastic Cushions

Snug makes loose false teeth fit firm and tight. Soothes sore gums due to loose fitting dentures. Harmless to plate. Easy to apply or remove Cushion. Long term use of an ill fitting denture, plate, pad or cushion may lead to swelling, faster bone resorption, or continuing irritation. Use SNUG temporarily until you can see your dentist.

Contents 2 Cushions

THE MENTHOLATUM CO., BUFFALO, N.Y. 14213

PD-214

Masius, Wynne-Williams, Street & Finney, Inc. EDITORIAL DEPARTMENT

IDENTIFICATION NO.

ADVERTISER: The Mentholatum Company

FOR: SNUG DENTURE CUSHIONS
"POWDERS & STICKUPS" (A)
(FSN-11-300)

DATE August 22, 1969

JOB NO. 1000TV33
As filmed: 8/19/69
As recorded: 8/22/69

	VIDEO	AUDIO
1.	OPEN ON CAN OF ADHESIVE POWDER, POURING POWDER ONTO LINED SURFACE.	1. ANNCR: (VO) Some people with l wobbly dentures___
2.	PULL BACK - ACTION CONTINUES.	2. ANNCR: (VO) use adhesive powde every morning and
3.	HAND SETS CAN ON SURFACE BEHIND SPRINKLE OF POWDER.	3. ANNCR: (VO) every night.
4.	BESIDE PILE OF POWDER, RIBBON OF ADHESIVE CREAM IS SQUEEZED OUT ONTO LINED SURFACE.	4. ANNCR: (VO) Others use cream
5.	TUBE OF CREAM IS SET DOWN BEHIND RIBBON. NOW BOTH PRODUCTS AND THEIR CONTENTS ARE SEEN SIDE BY SIDE.	5. ANNCR: (VO) day after day.
6.	THE CAN AND PILE OF POWDER POPS OFF.	6. ANNCR: (VO) But some never bot
7.	THE TUBE AND RIBBON OF CREAM POP OFF.	7. ANNCR: (VO) with daily fixing--
8.	CU PKG OF SNUG.	8. ANNCR: (VO) they line their de with Snug Brand De Cushions.
9.	PULL BACK AS HAND REMOVES CUSHION WITH BOTH LINERS ON FROM BOX. SUPER: "LASTS FOR WEEKS".	9. ANNCR: (VO) One lining lasts f weeks.
10.	WITH ONE LINER ON BACK, SHOWING SNUG CUSHION ON TOP, HAND BEGINS TO CUT SHAPE OF DENTURE.	10. ANNCR: (VO) Apply Snug at hom minutes.

IDINTIFICATION NO.

ADVERTISER The Mentholatum Company

FOR SNUG DENTURE CUSHIONS

"POWDERS & STICKUMS" (A)
(FSN-11-30C)

Page 2.

DATE August 22, 1969

JOB NO. 100T733
As filmed: 8/19/69
As recorded: 8/22/69

	VIDEO	AUDIO
11.	NOW "U" SHAPE OF DENTURE IS HELD IN HAND, WHILE BACKING LINER IS REMOVED. SUPER: "HOLDS DENTURES TIGHT".	11. ANNCR: (VO) It holds dentures tight
12.	HAND FLEXES CUSHION.	12. ANNCR: (VO) and cushions the gum lasts for weeks
13.	CUT BACK TO SET UP OF POWDER AND CREAM WITH CONTAINERS.	13. ANNCR: (VO) without daily fixing
14.	POWDER IS POPPED OFF.	14. ANNCR: (VO) Try the no-mess
15.	CREAM IS POPPED OFF.	15. ANNCR: (VO) no-bother way ...
16.	CU SNUG PACKAGE. SUPER: "HOLD DENTURES TIGHT". THEN POP ON: "2 CUSHIONS $1.50".	16. ANNCR: (VO) get Snug to hold dentures tight.

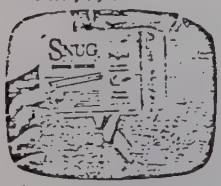
SNUG DENTURE CUSHIONS

TELEVISION COMMERCIAL, 1976-77
"SPOKESMAN"

1. SPOKESMAN: (DV) What do you use to hold loose wobbly dentures comfortably tight?

2. Powder?

3. Cream?



4. Or long-lasting Snug Brand Denture Cushions.

5. Snug is a cushion –

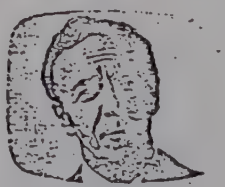
6. not only holds plates tight, but makes them feel so comfortable.

7. (VO) Easy to fit–

8. Snug sticks to your plates... lasts for weeks...

9. so no daily fixing...no mess... no after taste.

10. Easily cleaned or removed.



11. (DV) To hold dentures comfortably tight for weeks ...

12. (VO) get Snug Denture Cushions!

MASIUS, WYNNE-WILLIAMS INC.

CLIENT THE MENTHOLATUM COMPANY

TITLE "SPOKESMAN" (C) (ØMVSN2123) SNUG DENTURE CUSHIONS
:30 TV COMM'L. As Produced: 8/30/72
DATE 70 w As Filmed: 8/17/72
SEPT. 15, 1972

OPEN ON CU SPOKESMAN	SPOKESMAN (OC): What do you use to hold loose, wobbly dentures comfortably tight?
CUT TO CU AS HE SHAKES POWDER ON HIS PALM	Powder?
CU AS HE SQUEEZES CREAM ON PALM	Cream? Or long-lasting
CUT TO CU SNUG PKG AS HE PICKS IT UP	Snug Brand Denture Cushions.
HOLD CU AS HANDS SLIP OUT SNUG	Snug is a cushion --
PULL BACK TO MCU MAN	not only holds plates tight...but makes them feel so comfortable.
CUT TO CU MAN'S HANDS CUTTING SNUG INTO SHAPE WITH SCISSORS	Easy to fit...
DISS TO HIS HANDS FITTING U-SHAPED SNUG ONTO CLEAR LUCITE U-SHAPE	Snug sticks to your plat lasts for weeks...so no daily fixing...no mess.. no after-taste.
PAN AS HIS HANDS SCRUB SNUG ON LUCITE U-SHAPE, WITH TOOTHBRUSH UNDER RUNNING FAUCET	Easily cleaned or remove
CUT TO CU MAN	To hold dentures com-fortably tight for week:
CUT TO CU SNUG PKG	get Snug Denture Cushio:

SNUG DENTURE CUSHIONS

TELEVISION COMMERCIAL "SPOKESWOMAN"

1. SPOKESWOMAN: (DV) Thousands of denture wearers have long suffered

2. with loose, wobbly, uncomfortable plates.

3. Now many use Snug Brand Denture Cushions and

4. are so grateful for the way Snug holds dentures tight—

5. and being a cushion, Snug makes dentures feel so comfortable.

6. (VO) Easy to fit—

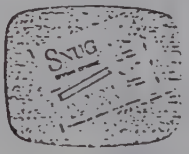
7. Snug sticks to your plates... lasts for weeks—

8. so no daily fixing—no mess—no after-taste.

9. (SFX) Easily cleaned

10 or removed.

11. (DV) To hold dentures comfortably tight for weeks...



12. (VO) get Snug Denture Cushions.

MASIUS, WYNNE-WILLIAMS INC.

CLIENT THE MENTHOLATUM COMPANY

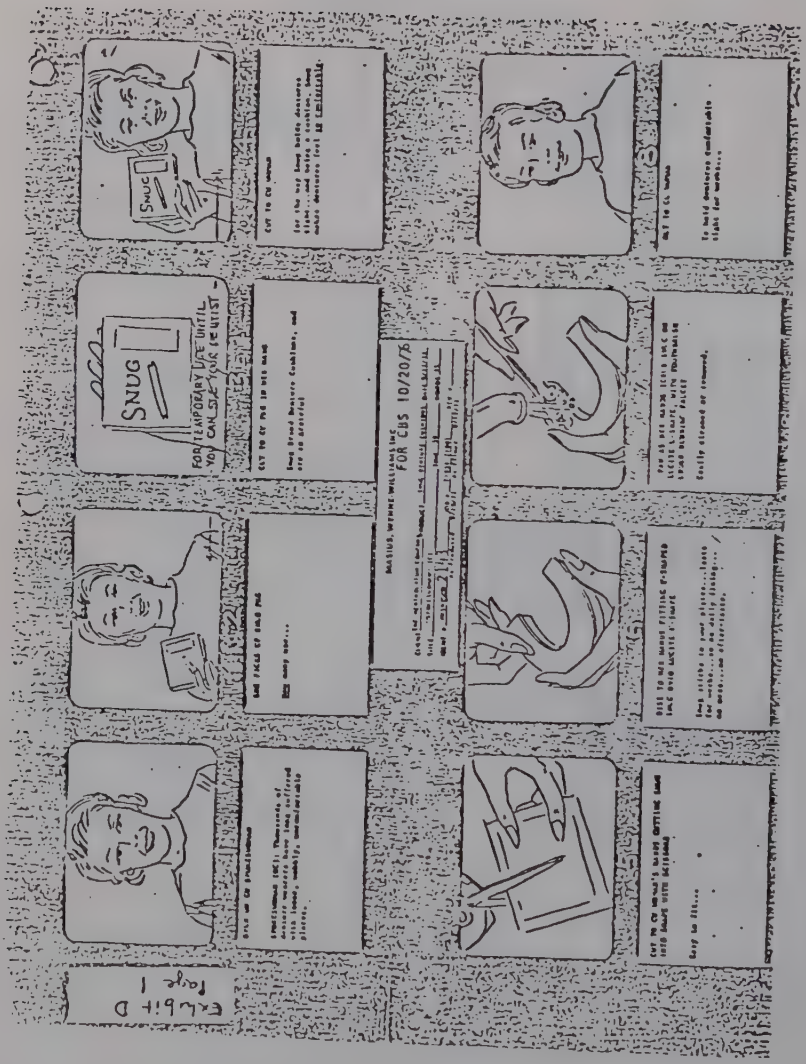
TITLE "SPOKESWOMAN" (C) (0MVSN2133)
:30 TV COMM'L

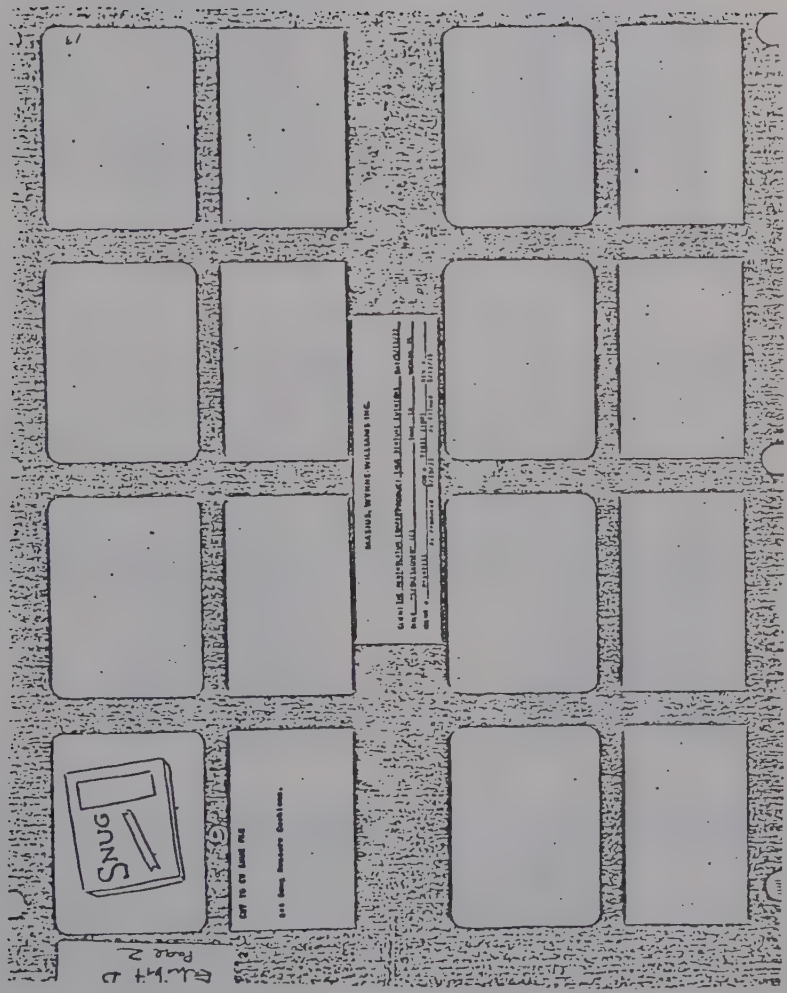
DATE SEPT 15, 1972

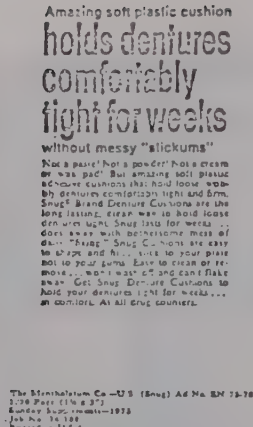
75 w

SNUG DENTURE CUSHIONS
As Produced: 8/30/72
As Filmed: 8/17/72

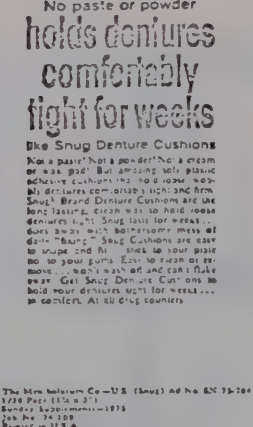
OPEN ON CU SPOKESWOMAN	SPOKESWOMAN (OC): Thousands of denture wearers have long suffered with loose, wobbly, uncomfortable plates.
SHE PICKS UP SNUG PKG	Now many use...
CUT TO CU PKG IN HER HAND	Snug Brand Denture Cushion and are so grateful
CUT TO CU WOMAN	for the way Snug holds dentures tight...and being a cushion, Snug makes dentures feel so comfortabl
CUT TO CU WOMAN'S HANDS CUTTING SNUG INTO SHAPE WITH SCISSORS	Easy to fit...
DISS TO HER HANDS FITTING U-SHAPED SNUG ONTO CLEAR LUCITE U-SHAPE	Snug sticks to your plates. lasts for weeks... so no daily fixing...no mess... no after-taste.
PAN AS HER HANDS SCRUB SNUG ON LUCITE U-SHAPE, WITH TOOTHBRUSH UNDER RUNNING FAUCET	Easily cleaned or removed.
CUT TO CU WOMAN	To hold dentures comfortabl tight for weeks...
CUT TO CU SNUG PKG	get Snug Denture Cushions.


SNUG
FOR TELEPHONE USE UNTIL YOU CAN SEE YOUR DENTIST -
FOR CBS 10/20/75
Exhibit D
Page 1


SNUG


Amazing soft plastic cushion
holds dentures comfortably tight for weeks
without messy "stickums"
Not a paste! Not a powder! Not a cream or wax pad! But amazing soft plastic adhesive cushions that hold loose wobbly dentures comfortably tight and firm. Snug® Brand Denture Cushions are the long lasting, clean way to hold loose dentures tight. Snug lasts for weeks ... does away with bothersome mess of daily "stickums." Snug Cushions are easy to shape and fit ... stick to your plate not to your gums. Easy to clean or remove ... won't wash off and can't flake away. Get Snug Denture Cushions to hold your dentures tight for weeks ... in comfort. At all drug counters.

The Sterilactum Co.—U.S. (Snug) Ad No. BN 75-703
3/30 Page (10" x 3")
Sunday Supplements—1975
Job No. 74-109
Printed in U.S.A.
D'ARCY-MacMANUS & MASIUS, Inc., New York


No paste or powder
holds dentures comfortably tight for weeks
like Snug Denture Cushions
Not a paste! Not a powder! Not a cream or wax pad! But amazing soft plastic adhesive cushions that hold loose wobbly dentures comfortably tight and firm. Snug® Brand Denture Cushions are the long lasting, clean way to hold loose dentures tight. Snug lasts for weeks ... does away with bothersome mess of daily "stickums." Snug Cushions are easy to shape and fit ... stick to your plate not to your gums. Easy to clean or remove ... won't wash off and can't flake away. Get Snug Denture Cushions to hold your dentures tight for weeks ... in comfort. At all drug counters.

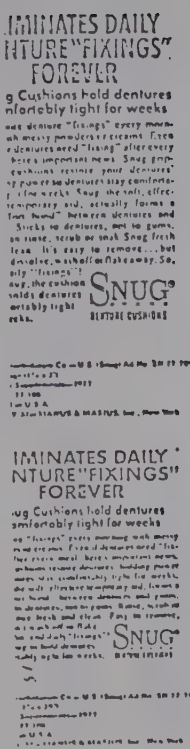
The Sterilactum Co.—U.S. (Snug) Ad No. BN 75-704
1/30 Page (10" x 3")
Sunday Supplements—1975
Job No. 74-109
Printed in U.S.A.
D'ARCY-MacMANUS & MASIUS, Inc., New York

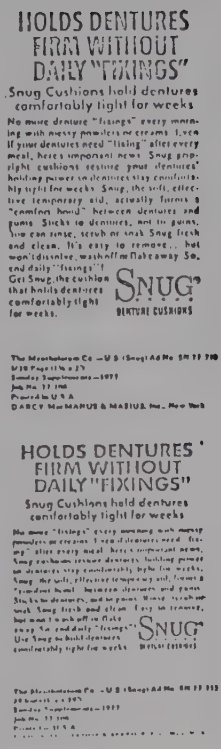
Amazing soft plastic cushion
holds dentures comfortably tight for weeks without messy "stickums"
Not a messy paste, powder, cream or wax pad—but an amazing soft plastic denture cushion. Snug® Brand Denture Cushions hold loose, wobbly dentures comfortably tight for weeks. With Snug there's no need to bother with messy, daily fixing. It lasts for weeks, sticks to your plate not to your gums so easy to clean or remove. Get Snug Denture Cushions to hold your dentures tight and firm for weeks ... in comfort. At all drug counters.

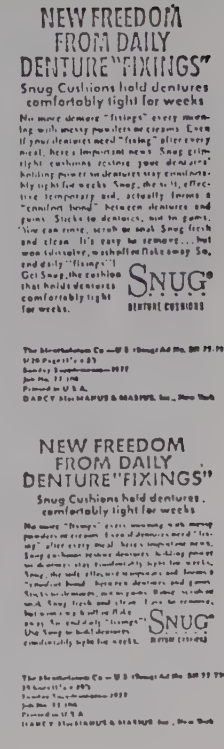
The Sterilactum Co.—U.S. (Snug) Ad No. BN 75-705
30 lines (10" x 3")
Sunday Supplements—1975
Job No. 74-109A
Printed in U.S.A.
D'ARCY-MacMANUS & MASIUS Inc. New York

No paste or powder
holds dentures comfortably tight for weeks like Snug Denture Cushions
Not a paste! Not a powder! Not a cream or wax pad! But amazing soft plastic adhesive cushions that hold loose, wobbly dentures comfortably tight for weeks. With Snug there's no need to bother with messy, daily fixing. It lasts for weeks, sticks to your plate not to your gums so easy to clean or remove. Get Snug Denture Cushions to hold your dentures tight and firm for weeks ... in comfort. At all drug counters.

The Sterilactum Co.—U.S. (Snug) Ad No. BN 75-706
30 lines (10" x 3")
Sunday Supplements—1975
Job No. 74-109A
Printed in U.S.A.
D'ARCY-MacMANUS & MASIUS Inc. New York


IMINATES DAILY
NTURE "FIXINGS".
FOREVER
g Cushions hold dentures
nfortably tight for weeks
SNUG
DENTURE CUSHIONS
IMINATES DAILY
NTURE "FIXINGS"
FOREVER
ug Cushions hold dentures
mfortably tight for weeks
SNUG


HOLDS DENTURES
FIRM WITHOUT
DAILY "FIXINGS"
Snug Cushions hold dentures
comfortably tight for weeks
SNUG
DENTURE CUSHIONS
HOLDS DENTURES
FIRM WITHOUT
DAILY "FIXINGS"
Snug Cushions hold dentures
comfortably tight for weeks
SNUG


NEW FREEDOM
FROM DAILY
DENTURE "FIXINGS"
Snug Cushions hold dentures
comfortably tight for weeks
SNUG
DENTURE CUSHIONS
NEW FREEDOM
FROM DAILY
DENTURE "FIXINGS"
Snug Cushions hold dentures
comfortably tight for weeks
SNUG

D'Arcy-MacManus & Masius
437 MADISON AVENUE
NEW YORK, NEW YORK 10022

Television Continuity

The Mentholatum Co.
ACCOUNT
Snug Denture Cushion
PRODUCT
"Movie"
TITLE
:30
LENGTH
MVSN 2153
SCRIPT NUMBER

As filmed 11/28/77

VIDEO		AUDIO
OPEN ON TWO WOMEN EXITING MOVIE HOUSE ONTO STREET	HELEN:	They don't make movies lik they used to.
WOMEN WALK DOWN STREET	SARA:	Let's have some of my pecs pie, that never changes.
CUT TO HELEN'S FACE, LOOKING EMBARRASSED.	HELEN:	Uh-Uh...It's been a while s I fixed my dentures...they' loose again.
2-SHOT AS SARA TALKS TO HELEN.	SARA:	Didn't I tell you about Snug?
ECU OF SNUG PACKAGE. WOMAN'S HAND PULLS CUSHION OUT. SUPER: 'FOR TEMPORARY USE UNTIL YOU SEE YOUR DENTIST."	SARA:	It's different -- you don't ne to apply it every day.
CUT TO HAND HOLDING DENTURE SHAPED LUCITE AS OTHER HAND PRESSES SHAPED CUSHION ONTO LUCITE.	SARA:	It's a cushion you just shape.
PALM DOWN HAND PRESSES AGAINST TOP OF LUCITE WHICH CLINGS TO HAND WITHOUT ANY OTHER SUPPORT.	SARA:	Snug lasts for weeks. And it hold your dentures firm and comfortable.
DISSOLVE TO SIMILAR SCENE AT A POINT LATER IN TIME.	SARA:	Pecan pie?
	HELEN:	Uh -- Uh --

D'Arcy-MacManus & Masius
437 MADISON AVENUE
NEW YORK, NEW YORK 10022

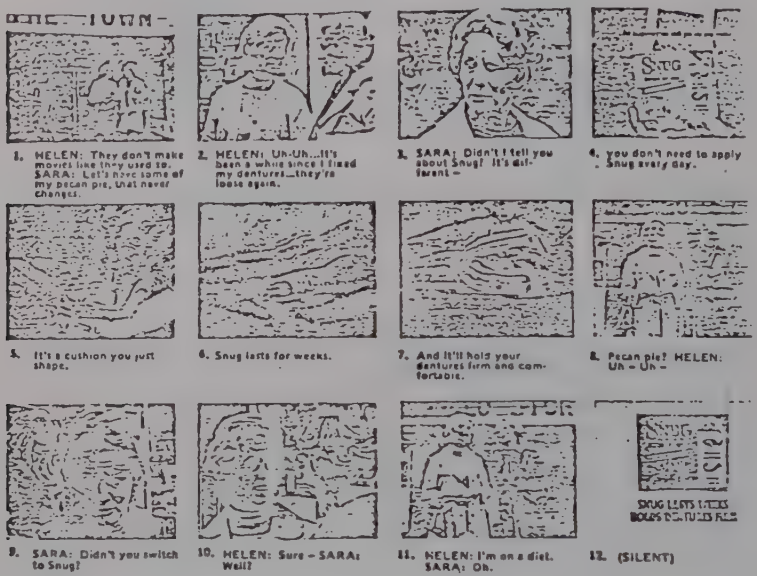
Television Continuity

The Mentholatum Co.
ACCOUNT
Snug Denture Cushio
PRODUCT
"Movie"
TITLE
:30
LENGTH
MVSN 2153
SCRIPT NUMBER

VIDEO	AUDIO
SCENE CONTINUES	HELEN: Sure --
	SARA: Well?
	HELEN: I'm on a diet.
ECU SNUG PACKAGE	
SUPER: SNUG LASTS WEEKS HOLDS DENTURES FIRM	

D'Arcy-MacManus & Masius
Advertising

CLIENT: MENTHOLATUM
PRODUCT: SNUG
TITLE & FILM NO: "MOVIE" - MVSNZ153
FIRST USE: 3/27/78
LENGTH: 30 SECONDS


1. HELEN: They don't make movies like they used to. SARA: Let's have some of my pecan pie, that never changes.
2. HELEN: Uh-Uh...it's been a while since I fixed my dentures...they're loose again.
3. SARA: Didn't I tell you about Snug? It's different –
4. you don't need to apply Snug every day.
5. It's a cushion you just shape.
6. Snug lasts for weeks.
7. And it'll hold your dentures firm and comfortable.
8. Pecan pie? HELEN: Uh – Uh –
9. SARA: Didn't you switch to Snug?
10. HELEN: Sure – SARA: Well?
11. HELEN: I'm on a diet. SARA: Oh.
12. (SILENT)

Decision and Order

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondents named in the caption hereof, and the respondents having been furnished thereafter with a copy of a draft of complaint which the bureau proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondents with violation of the Federal Trade Commission Act; and

The respondents, their attorneys, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondents of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondents that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondents have violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent Mentholatum Company is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its office and principal place of business located at 1360 Niagara St. in the City of Buffalo, State of New York.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

Order

I.

It is ordered, That respondent, the Mentholatum Company, a corporation, its successors and assigns, and its officers, agents, representatives and employees, directly or through any corporation, subsidiary, division or other device [hereinafter, "respondent"], in connection with the advertising, offering for sale, sale or distribution of any dental device or dental product, forthwith cease and desist

from disseminating or causing the dissemination of any advertisement by any means in or affecting commerce which makes any representation directly or indirectly that is inconsistent with, negates or contradicts any statement concerning matters of health, safety or efficacy set forth on the labeling of any such device or product or which in any way limits, qualifies or detracts from any such statement appearing on the labeling of any such device or product.

II.

It is further ordered, That respondent, in connection with the advertising, offering for sale, sale or distribution of any dental device or dental product (except denture cushions as provided for in Paragraph 3), shall, in disseminating or causing the dissemination by any means in or affecting commerce of any advertisement which makes any representation directly or indirectly (other than those prohibited in I above) regarding duration of use of any such product, disclose clearly and conspicuously any labeling warning regarding duration of use of such device or product.

It is agreed, for the purposes of this Order, that in the event a label or packaging warning regarding duration of use is no longer utilized for any such product, advertisements for said dental device or product need not bear a disclosure regarding duration of use.

III.

It is further ordered, That respondent, in connection with the advertising, offering for sale, sale or distribution of the product Snug Denture Cushions or any other denture cushion, when making any representation regarding the duration of use of said product (other than those prohibited in I, above), shall disclose clearly and conspicuously that said product is only appropriate for short-term use until a denture wearer is able to see a dentist for the adjustment of his or her loose or ill-fitting dentures. For the purposes of this Order, it is agreed that respondent may use the term "for weeks" in the advertising of denture cushion products so long as the terms "temporary" and "only until a dentist can be seen" are included, and the advertisement does not imply the product should be used on a long-term basis.

It is further agreed, for the purposes of this Order, that in the event that the Snug Denture Cushion product is no longer regarded by the federal Food and Drug Administration as suitable only for

short-term, non-regular use, the respondent may seek from the Commission amendment of this portion of this Order.

IV.

It is further ordered, That respondent shall forthwith distribute a copy of this Order to each of its operating divisions.

It is further ordered, That respondent notify the Commission at least thirty (30) days prior to any proposed change in its corporate status such as dissolution, emergence of a successor corporation, the creation or dissolution of any subsidiaries, and assignment or sale of the business, or any other change in the corporate respondent that may affect compliance obligations arising out of this Order.

It is further ordered, That respondent shall, within sixty (60) days after this Order becomes final, and annually thereafter for three (3) years, file with the Commission a report, in writing, signed by respondent, setting forth in detail the manner and form in which it has complied with this Order.

336-345 O - 81 - 50

IN THE MATTER OF

ENCYCLOPAEDIA BRITANNICA, INC., ET AL.

MODIFYING ORDER IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket 8908. Decision, March 9, 1976—Modifying Order, Oct. 28, 1980

This order modifies Paragraphs II(A), (B), (D) and (E) of the original Commission order issued March 9, 1976 (41 FR 19301, 87 F.T.C. 421) against respondents. The modifications permit respondents, for a one-year period, to use alternative means of making prescribed disclosures regarding their sales solicitation activities. This action affords respondents further opportunity to propose provisions that will lessen any undue financial impact on them and to demonstrate to the Commission that these provisions will effectively communicate to prospective customers, the disclosures required by the previous order.

ORDER MODIFYING CEASE AND DESIST ORDER

On March 9, 1976, the Commission issued an Order in this docket against Encyclopaedia Britannica, Inc., a corporation, and Britannica Home Library Services, Inc., a corporation. The Order includes, *inter alia,* provisions (Paragraphs II(A) and II(B)) requiring respondent, Encyclopaedia Britannica, Inc., to disclose in certain advertising and in a specified manner that persons who reply as requested may be contacted by a salesperson for the purpose of selling respondent's products. Furthermore, the Order (Paragraphs II(D) and II(E)) requires that when a sales representative of the respondent visits the home or place of business of potential purchasers of respondent's products, such representatives shall, at the time admission is sought, present a 3 by 5 card which identifies the sales representative and discloses that the purpose of the visit is to sell respondent's products.

On August 2, 1979, the United States Court of Appeals for the Seventh Circuit affirmed and enforced the Commission Order in this docket. On March 17, 1980, the Supreme Court of the United States denied respondents' petition for *certiorari.* Accordingly, pursuant to Section 5(g)(3) of the Federal Trade Commission Act, as amended, the Order of the Commission in this docket is now final.

During the time their *certiorari* petition was pending in the Supreme Court, respondents initiated discussion with the staff of the Commission concerning possible modifications of Paragraphs II(A), II(B), II(D) and II(E) of the Commission's Order. On March 18, 1980, Paragraphs II(A), (B), (D), and (E) of the Commission's Order were

stayed until further notice in order to permit the Commission to consider proposed modifications. On March 26, 1980, respondents filed their "Request to Reopen Proceedings and Modify Order." Respondents filed a memorandum in support of this request on May 2, 1980. In their petition and supporting memorandum, respondents asserted that, without such modifications, they would be placed at a competitive disadvantage, resulting in substantial financial harm to their business operations. Respondents also asserted that they have adopted in the last several years new sales procedures, including disclosures in advertising and in business calling cards presented by salespersons at the door of prospective customers, which effectively disclose to prospective customers the direct sales solicitation purpose and nature of such sales activities.

Pursuant to Section 2.51 of its Rules of Practice, the Commission invited public comment on respondents' petition to modify the Order. Having considered respondents petition and supporting memorandum, and the comments received, the Commission has determined that it would be appropriate to provide respondents further opportunity to (1) propose provisions that would lessen any undue financial impact on them and (2) present evidence demonstrating that such provisions will effectively communicate the information required by the original Order. Furthermore, with respect to the advertising disclosures required by Paragraphs II(A) and II(B), the Commission has determined that, without necessity of further evidence, certain modifications of the advertising disclosures can be ordered which will communicate effectively while allowing respondents alternative methods of making the disclosures.

Therefore, it is ordered, That Paragraphs II(A), (B), (D) and (E) of the Order issued in this docket on March 9, 1976 shall be modified as follows:

1. Paragraph II(A) shall read:

A. Disseminating or causing to be disseminated any advertisement or promotional material which solicits participation in any contest, drawing or sweepstakes, or solicits any response to any offer of merchandise, service or information, unless any such solicitation clearly and conspicuously discloses that a person who replies as requested may be contacted directly by a salesperson for the purpose of selling respondent's products, using one of the following disclosures:

1. IMPORTANT: This card will let you know of my interest and enable your [location designation, if appropriate] sales representative to

(contact me at home)		(information)
(call or visit me)	with	(details)
(contact me in person)		(facts)

on how I may (purchase) [applicable product].
(buy)

2. IMPORTANT: Returning this card allows me to have your [location designation, if appropriate] sales representative

(contact me at home)		(information)
(call or visit me)	with	(details)
(contact me in person)		(facts)

on how I may (purchase) [applicable product].
(buy)

3. IMPORTANT: Returning this card will enable your [location designation, if appropriate] sales representative to

(contact me at home)		(information)
(call or visit me)	with	(details)
(contact me in person)		(facts)

on how I may (purchase) [applicable product].
(buy)

Upon prior approval in writing of the Assistant Director of the Division of Compliance of the Bureau of Consumer Protection, or his designee, respondent may use any other disclosure that clearly and conspicuously discloses that a person who replies as requested may be contacted directly by a salesperson for the purpose of selling respondent's products. A request for approval shall be in writing and shall be deemed granted if not disapproved within 30 days after receipt by the Assistant Director of the Division of Compliance of the Bureau of Consumer Protection.

2. Paragraph II(B) shall read:

B. Providing any return card, coupon or other device which is used to respond to any advertisement or promotional material covered by Paragraph II(A) above, unless one of the disclosures set forth in such Paragraph, or a disclosure approved by the Assistant Director of the Division of Compliance or his designee as satisfying the requirements of Paragraph II(A), clearly and conspicuously appears in immediate proximity to the space provided for a signature or other identification of the responding party. During the one (1) year period from the date this Order become final, respondent may submit a request to reopen these proceedings pursuant to Section 2.51 of the Commission's Rules of Practice. Such petition shall contain information demonstrating that any proposed modifications of Paragraphs II(A) and II(B) will clearly and conspicuously disclose to potential purchasers of respondent's products that a person who replies as requested may be contacted directly by a salesperson for the purpose of selling respondent's products. The foregoing sentence shall not be construed as a limitation on respondent's submission of additional information regarding the request to reopen, including information relating to the financial impact of Paragraphs II(A) and II(B) on respondent. Should a request be submitted, the Commission shall determine whether to reopen these proceedings within one hundred-twenty (120) days of receipt of such request. The procedure to reopen the proceedings as set forth herein is in addition to, and not in lieu of, any

other procedure (or time period with respect to such procedure) permitted by law or the Commission's Rules of Practice.

3. Paragraph II(D) shall be amended by adding the following proviso at the end thereof:

Provided, however, that for one (1) year from the date this Order becomes final, respondent may, in lieu of the card required by this Paragraph of the Order, substitute a business card of at least 2 inches by 3-1/2 inches containing only the following information:

(1) the name of the corporation
(2) the name of the salesperson
(3) the term "sales representative"
(4) An address and telephone number at which the corporation or salesperson may be contacted
(5) the product or the corporation logo or identifying mark.

During this one (1) year period, respondent shall comply in all other respects with the requirements of Paragraph II(D) above. Prior to the expiration of the aforesaid time period, respondent may submit a request to reopen these proceedings pursuant to Section 2.51 of the Commission's Rules of Practice. Such petition shall contain information demonstrating that the business card required in Paragraph II(D), as modified above, is effective in communicating to potential purchasers, prior to the entry into their homes or places of business by any of respondent's sales representatives, that the purpose of the sales representative's call is to solicit the sale of respondent's products. The foregoing sentence shall not be construed as a limitation on respondent's submission of additional information regarding the request to reopen, including information on the financial impact of Paragraph II(D) on respondent. Should a request be submitted, the Commission shall determine whether to reopen these proceedings within one hundred-twenty (120) days of receipt of such request. Respondent may continue to use the business card, as described by this *proviso,* during the time that a request to reopen these proceedings pursuant to this Paragraph is pending, and, if such proceedings are reopened, until the Commission determination of the matter has become final. The procedure to reopen the proceedings as set forth herein is in addition to, and not in lieu of, any other procedure (or time period with respect to such procedure) permitted by law or the Commission's Rules of Practice.

4. Paragraph II(E) shall be amended by striking the words "to direct each such person to read the information contained on such card." The amended Paragraph shall read:

E. Failing to give the card, required by Paragraph II(D) above, to each person and to provide each such person with an adequate opportunity to read the card before engaging any such person in any sales solicitation.

It is further ordered, That the foregoing modifications shall become effective upon service of this Order.

It is further ordered, That the stay issued on March 18, 1980 shall be vacated and Paragraphs II(A), (B), (D) and (E), as modified by this Order, shall have full force and effect upon service of this Order.

Commissioner Pitofsky did not participate.

IN THE MATTER OF

UNIVERSAL BODYBUILDING, INC., ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT

Docket C-3048. Complaint, Nov. 5, 1980—Decision, Nov. 5, 1980

This consent order requires, among other things, a Redford, Mich. seller of various bodybuilding and self-improvement courses and products to cease from using adult models and testimonials in advertisements directed to non-adults; and advertising or promoting the sale of bodybuilding products or courses, unless it has tests or studies available which indicate that unsupervised use of its products will not be harmful to non-adults. The firm is further prohibited from making any unfair, deceptive or unsubstantiated product claim in advertising or other promotional material; and required to maintain specified records for a particular period.

Appearances

For the Commission: *Deandra Kraus.*

For the respondent: *Richard B. Poling, Jr., Moore, Sills, Poling, Wooster & Sinn,* Birmingham, Mich.

COMPLAINT

The Federal Trade Commission has reason to believe that Universal Bodybuilding, Inc., a corporation, and Morris Mitchell, individually and as an officer of Universal Bodybuilding, Inc., have violated the provisions of the Federal Trade Commission Act. It appears to the Commission that a proceeding by it would be in the public interest. The Commission hereby issues its complaint as follows:

PARAGRAPH 1. Respondent Universal Bodybuilding, Inc. is a corporation with its principal office and place of business located at 26903 West Eight Mile Road, Redford, Michigan.

Respondent Morris Mitchell is president of Universal Bodybuilding, Inc. He formulates, directs and controls the policies, acts and practices of Universal Bodybuilding, Inc. His address is the same as that of Universal Bodybuilding, Inc.

All allegations made in the present tense include the past tense.

PAR. 2. In the conduct of their business, respondents sell bodybuilding, muscle-building and other self-improvement courses, devices, and products (hereafter products) directly to the purchasing public, including young people under 17 years of age (non-adults),

through the mail in various States of the United States and in the District of Columbia.

PAR. 3. To promote the sale of their products, respondents prepare, or cause to be prepared, advertisements which they publish or cause to be published in various publications, including publications directed to and read primarily by non-adults, which are distributed throughout the United States.

PAR. 4. Typical but not all inclusive of such advertisements are the following:

FREE
Booklet
SEE YOUR MUSCLES GROW DAY BY DAY
TAKE YOUR CHOICE! You Can Do This...
BUILD POWERFUL MUSCLES...FAST!
LOSE FAT!
GAIN MUSCULAR WEIGHT!
DOUBLE OR TRIPLE YOUR STRENGTH!
TRIM YOUR WAIST!
FEEL BETTER
YOU'LL PUT ON INCHES OF POWERFUL MUSCLES ON YOUR BODY!
Our New System will develop muscles so fantastic that your muscles and strength will seem to be almost Super-Human! Thousands have doubled or tripled their strength while following our unique methods. It is actually possible to have everyday muscular growth while following our body building system! Imagine what you could accomplish while following our methods? Regardless of the shape you're in, WE CAN IMPROVE YOUR BODY 100%! Your own friends won't recognize your body when we get done with it. FANTASTIC, BUT TRUE!
GET INTO SHAPE
LIKE MORE FACTS?
Shape-Up, Get that waistline down and muscularize it!
SKINNY? MUSCLES WILL APPEAR ... ALMOST LIKE MAGIC!
FAT? FAT WILL DISAPPEAR — REPLACED BY MUSCLES!
YOUR NEW MUSCLES WILL FEEL LIKE DYNAMITE!
FREE
Universal, Dept. MAR-1
Box 8894
Detroit, Mich. 48240
You bet I want MUSCLES - rush me your FREE Booklet and all your Colorful Brochures!! I am sending you 25c to help cover postage and handling costs. (please PRINT clearly)
Name
Age
Address
City
State
Zip
MAIL THIS COUPON TODAY

Super

BODYBUILDING COURSE—

INTRODUCING

THE BODYBUILDING SYSTEM THAT GUARANTEES —

YOU'LL PUT ON INCHES OF POWERFUL MUSCLES ON YOUR BODY!

At last, NEW bodybuilding secrets are now available for your use. Finally, after years of experimenting we have come up with the fastest muscle building system in the world. Our course really works — thousands have taken our course and have obtained fantastic results. Right in the privacy of your own bedroom you can completely transform your body.

DISCOVER THE SECRET SYSTEM!

You Can have POWERFUL MUSCLES FAST . . . not by years and years of hard work . . . but by simply following our fascinating system . . . a system that works so fast you can see results from day to day! Isn't that the kind of course you want? We absolutely guarantee results.

HERE ARE JUST A FEW OF THE LETTERS WE HAVE RECEIVED

"Wow! I am making fantastic gains following your new method of muscle building. I never knew it could be so easy to build muscles."
J. Johnson

"In just 3 weeks I have gained 1½" on my arms and 4" on my chest. I have also lost 4" off my waist. Your course is just great."
D. Roberts

"I was a skinny weakling when I enrolled. Now I've gained 30 pounds in just 45 days. I am truly amazed. I am going to be dynamite on the beach."
B. Abbott

"I'm transforming all the fat off my body and changing it into rock hard muscle. It's amazing. I have lost 8" off my waist. I can actually see my muscles growing from day to day."
P. Williams

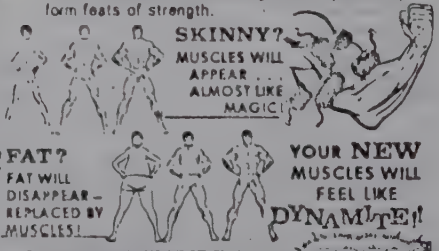
"I have gained 20 pounds in just 30 days and I have gained over 5 inches on my chest. I find that my power has doubled. In sports I am a winner in everything I do."
B. Daniels

"I have gained 5" on my arms and 12" on my chest while losing 3" off my waist. I have tripled my power and speed. Thanks for what you have done for me."
W. Robinson

MORRIE MITCHELL GAINED 65 POUNDS OF MUSCLE WHILE FOLLOWING OUR "REVOLUTIONARY NEW METHODS" ON BODYBUILDING.

TAKE YOUR CHOICE! You Can Do This...

★ DOUBLE OR TRIPLE YOUR STRENGTH in record time! It wouldn't take long before you can perform feats of strength.


SKINNY?
MUSCLES WILL APPEAR . . . ALMOST LIKE MAGIC!
FAT?
FAT WILL DISAPPEAR — REPLACED BY MUSCLES!
YOUR NEW MUSCLES WILL FEEL LIKE DYNAMITE!

FREE

Universal Bodybuilding
Box 6268 Dept CHA
Detroit, Mich 48240

Shoot the works to me free! Rush me all that free muscle-building information, so that I can add inches of powerful muscles — all in the privacy of my home. I am sending 25¢ to help cover postage and handling costs. I am under no obligation. (Please print)

Name _____ Age _____

Address _____

City _____ State _____ Zip _____

MAIL THIS COUPON TODAY

PAR. 5. By and through the preceding advertisements and other advertisements, respondents represent, directly or by implication, that a typical consumer who is likely to respond to respondents' advertisements will attain rapid improvement in his physical appearance, add muscles, lose fat and gain respect from his peers.

PAR. 6. By and through the preceding advertisements and other similar representations, respondents represent, directly or by implication, that the Universal Bodybuilding System:

1. makes muscles appear quickly and easily, with little effort;
2. is 200% to 300% more effective in muscle-building than any form of isometrics; and
3. is the fastest muscle-building system in the world.

This list is representative, but not all inclusive, of the representations made by respondents.

PAR. 7. By and through the preceding advertisements and other similar advertisements, respondents represent, directly or by implication, that the endorsements presented in the advertisements represent the typical and expected results of use of respondents' products in the manner depicted in the advertisement by a typical consumer who is likely to respond to respondents' advertisements.

PAR. 8. By and through the preceding advertisements and other advertisements, respondents represent, directly or by implication, that the physical stature of the models featured in the advertisements is attainable through use of respondents' products in the manner depicted in the advertisements by a typical consumer who is likely to respond to respondents' advertisements.

PAR. 9. By and through the preceding advertisements and other advertisements, respondents represent, directly or by implication, that they have, and rely on, competent scientific tests or studies sufficient to provide a reasonable basis to believe that the above representations are true.

PAR. 10. By and through the preceding advertisements and other advertisements directed to and read primarily by non-adults, respondents represent that use of respondents' products without appropriate supervision will not be harmful to non-adult consumers.

PAR. 11. In truth and in fact and in contradiction to the representations of respondents:

A. Use of respondents' products will not allow a typical consumer who is likely to respond to respondents' advertisements to rapidly attain a change in physical appearance, add muscles, lose fat or command respect from everyone he meets.

In addition:

1. the Universal Bodybuilding System does not make muscles appear quickly and easily, with little effort;
2. the Universal Bodybuilding System is not 200 to 300 percent more effective in muscle-building than any form of isometrics; and
3. the Universal Bodybuilding System is not the fastest muscle-building system in the world.

B. The endorsements presented in respondents' advertisements do not represent the typical and expected results of use of respondents' products in the manner depicted in the advertisements by a typical consumer who is likely to respond to respondents' advertisements.

C. The physical stature of the models featured in these advertisements is not attainable through use of respondents' products in the manner depicted in the advertisements by a typical consumer who is likely to respond to respondents' advertisements.

D. Respondents, at the time such representations were made, did not possess and rely on competent substantiation sufficient to provide a reasonable basis to believe that the representations were true.

E. Respondents, at the time the representation in Paragraph Ten was made, did not have, and rely on, competent scientific tests or studies sufficient to provide a reasonable basis to believe that use of respondents' products without appropriate supervision will not be harmful to non-adult consumers.

Therefore, the advertisements referred to above are unfair and deceptive.

PAR. 12. To promote the sale of their products, respondents disseminate advertisements which are directed to non-adults and which are read by an audience which is primarily composed of non-adults. In these advertisements, respondents make use of pictures or drawings of professional adult bodybuilding or weight-lifting models to promote their products. The physical stature of the models depicted in these advertisements is unattainable by the non-adults who read them. In these advertisements, respondents also make use of testimonials of adults who have used respondents' products. The results achieved by these adults cannot be achieved by the non-adults who read these advertisements.

PAR. 13. The use by respondents of the pictures or drawings described in Paragraph Twelve has the tendency and capacity to

mislead non-adults as to the results they might achieve through use of respondents' products.

PAR. 14. The use by respondents of testimonials which relate the experience of adults who have used respondents' products as related in Paragraph Twelve has the tendency and capacity to mislead non-adults to believe that they will experience similar results.

Therefore, the advertisements referred to in Paragraph Twelve are unfair and deceptive.

PAR. 15. The use by respondents of these unfair and deceptive advertisements has the tendency and capacity to mislead consumers, especially non-adults, into erroneous and mistaken beliefs regarding the results of use of respondents' products and to purchase substantial quantities of respondents' products by reason of these erroneous and mistaken beliefs.

PAR. 16. The acts and practices of respondents, as alleged in the preceding paragraphs, are all to the prejudice and injury of the public and constitute unfair and deceptive acts and practices in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act, as amended.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondents named in the caption hereof, and the respondents having been furnished thereafter with a copy of a draft of complaint which the Seattle Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondents with violation of the Federal Trade Commission Act; and

The respondents, their attorneys, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondents of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondents that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondents have violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further

conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent Universal Bodybuilding, Inc. is a corporation with its principal office and place of business located at 26903 West Eight Mile Road, Redford, Michigan.

Respondent Morris Mitchell is president of Universal Bodybuilding, Inc. He formulates, directs and controls the policies, acts and practices of Universal Bodybuilding, Inc. His address is the same as that of Universal Bodybuilding, Inc.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents, and the proceeding is in the public interest.

ORDER

This order applies to respondent Universal Bodybuilding, Inc., a corporation, its successors and assigns and its officers, agents, representatives and employees, in connection with offering for sale, sale or distribution of any bodybuilding, muscle-building or other self-improvement products, devices or courses directly or through any corporation, subsidiary, division, or other device in or affecting commerce, as commerce is defined in the Federal Trade Commission Act, as amended. This order applies to respondent Morris Mitchell in connection with advertising, offering for sale, sale or distribution of any bodybuilding, muscle-building or other self-improvement products, devices or courses in or affecting commerce, as commerce is defined in the Federal Trade Commission Act, as amended. This order shall not apply to Morris Mitchell insofar as he is involved only in the bona fide sale of advertising services to businesses which are not involved in the sale or offering for sale of any bodybuilding, muscle-building, or other self-improvement products, devices or courses and in which he or members of his immediate family have no financial interest.

For purposes of this order "non-adults" shall mean persons under 17 years of age. Advertisements directed to non-adults shall mean all advertisements and promotional material:

1. whose dominant appeal is to non-adults;
2. mailed directly to a person who respondent has reason to believe is a non-adult; or
3. disseminated in publications whose audience for the prior 12 months was composed of a majority of non-adults.

Such publications shall include all comic books, *Mad Magazine, Boy's Life, Children's Digest* and *Jack and Jill.* This list is intended to be representative of publications covered by this order but not exclusive.

I.

It is ordered, That in all advertisements directed to non-adults respondents cease and desist from:

A. Advertising or in any way promoting the sale of bodybuilding or muscle-building products, devices or courses (hereafter referred to as products) until respondents have available and rely on competent scientific or medical tests or studies adequate to show that use of the products without appropriate supervision will not be harmful to non-adult consumers.

B. Using pictures or drawings of adults or professional models to promote the sale of bodybuilding or muscle-building products.

C. Making any representation, directly or by implication, unless, at the time the representation is made, respondents have, and rely on, substantiation sufficient to provide a reasonable basis to believe that the representation is true for the typical non-adult consumer of respondent's products. In interpreting this provision, respondents shall not represent that a consumer can achieve any result unless and until respondents can substantiate by competent tests or studies that the result can be attained by a typical non-adult who uses the product in the manner depicted in the advertisement. The original data collected for any such studies performed at the request of or with the financial assistance of respondents and a detailed description of how the test or study was performed must be available for inspection by the Federal Trade Commission for at least two years following the final use of the representation.

D. Using any testimonial which does not represent the typical experience of non-adult consumers of respondents' products.

E. Making any representation, directly or indirectly, which exaggerates or overstates the results which may reasonably be expected to result from use of any product by a non-adult.

II.

It is further ordered, That in all advertisements respondents cease and desist from:

A. Representing in any manner, directly or by implication,

including through the use of testimonials, that a typical consumer who uses respondents' products will attain rapid improvement in his physical appearance, add muscles, lose fat or gain respect from his peers unless the representation is, in fact, true.

B. Representing in any manner, directly or by implication, that any product:

(1) Makes muscles appear quickly and easily, with little effort;

(2) Is more effective than isometrics or any other form of muscle-building, bodybuilding or self-improvement products;

unless the representation is, in fact, true.

C. Disseminating any advertisement or promotional material which contains unfair or deceptive representations or fails to disclose material facts regarding the advertised product(s).

D. Making any representation, directly or by implication, unless at the time the representation is made, respondents have, and rely on, substantiation sufficient to provide a reasonable basis to believe that the representation is true for the typical consumer of respondents' products. In interpreting this provision, respondents shall not represent that a consumer can achieve any result unless and until respondents can substantiate by competent tests or studies that the result can be attained by a typical consumer who uses the product in the manner depicted in the advertisement. The original data collected for any such studies performed at the request of or with the financial assistance of respondents and a detailed description of how the test or study was performed must be available for inspection by the Federal Trade Commission for at least two years following the final use of the representation.

Provided that respondents may use testimonials which do not represent the typical experience of consumers of respondents' product(s) if (1) the testimonial itself is truthful; and (2) all conditions which contributed to the atypical results are clearly and conspicuously disclosed. Such conditions shall include, but shall not be limited to, the prior physical condition of the user, use of a special diet, use of bodybuilding products in addition to the advertised products and use of the product in a manner which differs from that depicted in the advertisement (*e.g.*, use of the product for a longer period of time each day than advertised).

E. Representing in any manner, directly or by implication, that the physical stature of any model used in an advertisement is attainable by typical consumers who use the product unless it is, in fact, attainable.

III.

It is further ordered, That respondents maintain complete business records relative to the manner and form of their compliance with this order. Respondents shall retain each such record for at least three years, and shall retain substantiation and other documentation at least two years beyond the last dissemination of any representation or testimonial which relies on the substantiation under the provisions of this order. Upon reasonable notice, respondents shall make any and all such records available for inspection and photocopying by authorized representatives of the Federal Trade Commission at respondents' place of business or other properly designated location.

IV.

It is further ordered, That respondent Universal Bodybuilding, Inc., shall immediately deliver a copy of this order to each operating division and affiliated business. Respondent Universal Bodybuilding, Inc., shall also immediately deliver a copy of this order to all personnel now or hereafter engaged in the sale or offering for sale of respondents' services or in any aspect of the preparation, creation or placing of advertising on behalf of respondents. Respondents shall secure from each such person a signed statement acknowledging receipt of the order.

V.

It is further ordered, That respondents notify the Commission at least thirty days prior to any proposed change in a corporate respondent, such as dissolution, assignment or sale resulting in the emergence of a successor corporation or corporations, the creation or dissolution of subsidiaries, or any other change in the corporations which may affect compliance obligations arising out of the order.

It is further ordered, That Morris Mitchell promptly notify the Commission of the discontinuance of his present business or employment and of his affiliation with a new business or employment relating to the promotion or sale of body building, muscle-building or self-improvement courses, devices or products. In addition, for a period of 10 years from the date of service of this order, he shall promptly notify the Commission of each affiliation with such a new business or employment. Each such notice shall include his new business address and a statement of the nature of the business or employment in which he is newly engaged as well as a description of

336-345 O - 81 - 51

his duties and responsibilities in connection with the business or employment. The expiration of the notice provision of this paragraph shall not affect any other obligation arising under this order.

VI.

It is further ordered, That the respondents herein shall, within sixty days after service of this order, file with the Commission a written report setting forth in detail the manner and form of their compliance with this order.

IN THE MATTER OF

GENSTAR LIMITED

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT AND SEC. 7 OF THE CLAYTON ACT

Docket C-3049. Complaint, Nov. 10, 1980—Decision, Nov. 10, 1980

This consent order requires, among other things, a Canadian corporation engaged in various business enterprises, including the manufacture and sale of portland cement and gypsum wallboard, to cease, for a prescribed period, from entering into or carrying out supply agreements with U.S. competitors that provide for the exchange of cost and pricing information and permit the firm to share in profits realized from the resale of its products in the United States. The firm is also prohibited, for a specified time, from selling or delivering to any "Cement Facility" for further processing or resale, products produced at company-owned cement manufacturing plants located outside the United States. Further, for each calendar year, beginning January 1, 1981 and ending December 31, 1984, respondent is required to make available for sale to manufacturers having cement facilities located in the "Northwest Cement Market," all cement or clinker produced at its plant at Tilbury Island, British Columbia, that is not sold to Canadian customers. Additionally, the firm is prohibited from acquiring, without prior Commission approval, any portland cement or gypsum wallboard manufacturing plant that is located within geographic areas set forth in the order.

Appearances

For the Commission: *Robert W. Mannix* and *Alfred J. Ferrogari.*

For the respondent: *Lucian C. Jones, Shearman & Sterling,* New York City.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act and the Clayton Act, as amended, and by virtue of the authority vested in it, the Federal Trade Commission, having reason to believe that Genstar Limited, a corporation subject to the jurisdiction of the Commission, has violated said Acts, and it appearing that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint and states its charges as follows:

I.

DEFINITIONS

1. For the purpose of this complaint the following definitions shall apply:

(a) *Portland cement* includes Types I through V of portland cement as specified by the American Society for Testing Materials.

(b) *Clinker* means a substance ranging in particle size from fine sand grains to walnut size which is formed by heating a properly proportioned mixture of raw materials containing calcium carbonate, silica, alumina and iron oxide in a kiln to a temperature at which fusion occurs. When ground and mixed with gypsum, clinker becomes portland cement.

(c) *Gypsum wallboard* includes gypsum lath, veneer base, gypsum sheathing, regular gypsum wallboard, type X gypsum wallboard, predecorated wallboard and other specialty gypsum wallboard items.

(d) The term *Northwest Cement Market* consists of Northern California, Western Oregon and Western Washington.

(e) The term *Northern California* refers to that part of California identified by the Bureau of Mines as Northern California (points north and west of the northern borders of San Luis Obispo and Kern Counties and the western borders of Inyo and Mono Counties).

(f) The term *Western Oregon* refers to all counties west of a dividing line following the eastern boundaries of Klamath, Lane, Linn, Marion, Clackamas and Hood River Counties and composed of the counties of Klamath, Lane, Linn, Marion, Clackamas, Hood River, Multnomah, Douglas, Jackson, Josephine, Curry, Coos, Benton, Lincoln, Yamhill, Tilamook, Washington, Clatsop, Polk and Columbia.

(g) The term *Western Washington* refers to all counties west of a dividing line following the eastern boundaries of Klickitat, Skamania, Lewis, Pierce, King, Snohomish, Skagit and Whatcom Counties and composed of the counties of Klickitat, Skamania, Clark, Cowlitz, Lewis, Pierce, King, Snohomish, Skagit, Whatcom, San Juan, Island, Kitsap, Mason, Thurston, Clallam, Jefferson, Grays Harbor, Pacific and Wahkiakum.

(h) The term *4-State Area* consists of Washington, Oregon, California and Nevada.

II.

GENSTAR LIMITED

2. Respondent Genstar Limited (hereinafter Genstar) is a Canadian corporation with principal offices at Suite 4105, One Place Ville Marie, Montreal, Quebec, Canada.

3. Genstar, through its divisions and subsidiaries, is engaged in the manufacture and sale of cement, including portland cement and gypsum wallboard. Genstar is also engaged in a variety of other business operations including substantial business operations in or affecting commerce of the United States.

III.

THE FLINTKOTE COMPANY

4. The Flintkote Company (hereinafter Flintkote) is a publicly held corporation, organized and existing under the laws of the State of Massachusetts with its principal office located at 1351 Washington Boulevard, Stamford, Connecticut.

5. Flintkote is engaged in the manufacture and sale of materials and products for the building and construction industries including, but not limited to, portland cement and gypsum wallboard.

IV.

JURISDICTION

6. At all times relevant herein, Genstar, through its divisions and subsidiaries, has been and is now engaged in interstate negotiations and transactions and has sold and shipped its products in interstate commerce. Genstar has engaged in "commerce" within the meaning of the Clayton Act and is a corporation whose business is in or affects commerce as "commerce" is defined in the Federal Trade Commission Act.

7. At all times relevant herein, Flintkote, through its divisions and subsidiaries, has been and is now engaged in interstate negotiations and transactions and has sold and shipped its products in interstate commerce. Flintkote has engaged in "commerce" within the meaning of the Clayton Act and is a corporation whose business is in or affects commerce as "commerce" is defined in the Federal Trade Commission Act.

V.

ACQUISITION

8. Between approximately June 1978 and September 1978, Genstar, through its indirectly wholly-owned subsidiary Dorster, Inc., purchased 1,450,000 shares of Flintkote Common Stock, $5.00 par value, representing approximately 21.5% of the outstanding voting shares of Flintkote (based upon 6,719,107 shares of Common Stock authorized and issued on June 30, 1978). All of the purchases of such shares were effected in open-market and negotiated transactions on the New York Stock Exchange with a substantial number of holders. On October 18, 1979, Genstar proposed to the board of directors of Flintkote that Genstar make a cash tender offer for all of the remaining outstanding shares of Flintkote.

9. The cost of the acquisition of the shares purchased on the open market was approximately $51,267,010.

10. Genstar's acquisition of approximately 21.5% of Flintkote's Common Stock gives it the power to: (a) influence and control Flintkote's business affairs; (b) influence the management of Flintkote in favor of a merger between the two companies; and/or (c) to provide a base from which to launch a tender offer.

VI.

TRADE AND COMMERCE

A. Portland Cement

11. A relevant line of commerce is the manufacture and sale of portland cement.

12. A relevant section of the country with respect to portland cement is the "Northwest Cement Market" as defined herein.

13. The manufacture and sale of portland cement in the Northwest Cement Market is concentrated. For the year 1978, total sales of portland cement, as defined herein, in the relevant market amounted to approximately 5.1 million tons. The four largest manufacturers had sales of approximately 3.5 million tons, or 69.6% of all sales; the eight largest manufacturers had sales of approximately 4.8 million tons, or 94.7% of all sales of portland cement.

14. Entry into the manufacture and sale of portland cement is difficult. A successful entrant must possess substantial financial resources, considerable technical expertise and a long-term supply of the necessary basic raw materials. An additional barrier to entry exists in the fact that existing environmental protection regulations

make it extremely difficult to obtain the necessary permits for new plant and terminal construction and operation as well as basic raw materials mining operations.

15. For the year 1978, Flintkote ranked third in sales of portland cement in the Northwest Cement Market with approximately 18.3% of all sales.

16. In 1978, Kaiser Cement and Gypsum Corporation (Kaiser), ranked first in sales of portland cement in the Northwest Cement Market and it accounted for approximately 24.4% of all sales.

17. In 1978, Lone Star Industries, Inc. (Lone Star) ranked second in sales of portland cement in the Northwest Cement Market with approximately 18.9% of all sales.

18. Flintkote is now, and has been, a significant competitor of Kaiser and Lone Star in the sale of portland cement in the Northwest Cement Market.

19. In late 1979 or early 1980, depending on when Genstar's newly constructed cement manufacturing facility at Tilbury Island, British Columbia achieves specified minimum production levels, executed long-term contracts for the sale of cement by Genstar to Kaiser and for the sale of clinker by Genstar to Lone Star will become effective.

20. The contract between Genstar and Kaiser calls for Kaiser to purchase 200,000 tons per year (TPY) of cement, substantially composed of portland cement, for ten years with an option exercisable by Kaiser to reduce volume by up to 40,000 TPY, in any of the last four years.

21. The contract with Kaiser, among other things, provides Genstar with a continuing interest in the profitability at which cement purchased from it by Kaiser is resold by Kaiser in the Northwest Cement Market, because it uses a pricing formula which includes a profit sharing feature in addition to a minimum guaranteed return to Genstar. Other provisions of the contract include exchanges of cost and price information, advance estimation as to the price at which Kaiser will resell cement purchased from Genstar and a guaranty to Kaiser of the most favored price for cement or clinker purchased by any customer of Genstar for resale in the states of Washington and Oregon.

22. The contract between Genstar and Lone Star calls for Lone Star to purchase clinker in amounts of 250,000 TYP in the first two years and 275,000 TPY in the next three years. The Lone Star contract is renewable at Lone Star's option for a second five-year term and provides for minimum purchases of clinker at the rate of

200,000 TPY for the first four years of the renewal period and 175,000 tons during the last year of the renewal period.

23. The contract with Lone Star provides, among other things, that Genstar's price to Lone Star will be determined in accordance with the formula for determining Genstar's price to Kaiser (less $1.50 per ton clinker allowance) and includes a minimum guaranteed return to Genstar equivalent to that provided by Kaiser. The Lone Star agreement also provides for inspection of the books and records of each party relating to any provision of the agreement, access to be given through independent auditors, with limited direct access in defined circumstances. Further, the contract defines events of hardship which, should any occur, the parties are in good faith obliged to attempt to resolve them, "even to the extent of sharing the economic burden occasioned by the hardship". The enumerated events of hardship include among other things, the failure of the contract price to afford Lone Star a minimum margin of U.S. $4.50 per ton on cement purchased from Genstar and resold in the Northwest Cement Market, the experience of unusual, severe and unforeseen difficulties in the manufacture of clinker or cement by Genstar or of cement by Lone Star; the occurrence of adverse market developments in the area traditionally serviced by Lone Star's Seattle plant, which causes Lone Star to cease the manufacture of clinker at its Seattle plant for an uninterrupted period of thirty days or more (in which case Lone Star shall be entitled to a ratable reduction in the contract tonnage it is obliged to take from Genstar on condition that it does not avail itself of another source of supply). Lone Star is also guaranteed the most favored price for cement or clinker purchased by any customer of Genstar for resale in the States of Washington and Oregon.

24. The contracts between Genstar and Kaiser and Genstar and Lone Star, either individually or as they operate in conjunction with each other, would constitute contracts, combinations or conspiracies in restraint of trade, if Genstar were a direct competitor in the Northwest Cement Market.

B. Gypsum Wallboard

25. A second relevant line of commerce is the manufacture and sale of gypsum wallboard.

26. A relevant section of the country with respect to gypsum wallboard is the "4-State Area" as defined herein.

27. The manufacture and sale of gypsum wallboard in the 4-State Area is concentrated. For the year 1978, total sales of gypsum wallboard, as defined herein, in the 4-State Area amounted to

approximately 2,959,290 MSF (MSF = 1000 square feet). The four largest manufacturers had sales of approximately 2,065,036 MSF, or 69.7% of all sales; the eight largest manufacturers had sales of approximately 2,891,012 MSF, or 97.7% of all sales of gypsum wallboard.

28. Entry into the manufacture and sale of gypsum wallboard is difficult. A successful entrant must possess substantial financial resources, considerable technical expertise and a long-term supply of the necessary basic raw materials. An additional barrier to entry exists in the fact that existing environmental protection regulations make it extremely difficult to obtain the necessary permits for new plant construction and operation as well as basic raw materials mining operations.

29. For the year 1978, Genstar ranked ninth in sales of gypsum wallboard with approximately 2.1% of all sales. During the same year, Flintkote ranked fourth in sales of gypsum wallboard with 14.6% of all sales. A combined Genstar-Flintkote would have ranked second with 16.7% of all gypsum wallboard sales in 1978.

VII.

EFFECTS OF THE ACQUISITION

30. The effect of Genstar's acquisition of Flintkote, a direct competitor of Kaiser and Lone Star, may be to create a combination in restraint of trade, which may substantially lessen competition or tend to create a monopoly in the Northwest Cement Market in the following ways:

(a) Actual price and other competition among Flintkote, Kaiser and Lone Star in the manufacture and sale of portland cement may be substantially reduced;

(b) Cooperation among Flintkote, Kaiser and Lone Star with respect to the production, distribution, pricing and/or sale of portland cement may be increased to the detriment of competition generally and/or have the effect of fixing, stabilizing or maintaining prices and/or have the effect of allocating markets or customers or restricting available supplies of portland cement in the Northwest Cement Market or sections thereof.

(c) Actual competition among competitors generally in the manufacture and sale of portland cement may be lessened.

31. The effect of Genstar's acquisition of Flintkote may be substantially to lessen competition or to tend to create a monopoly in

the manufacture and sale of gypsum wallboard in the 4-State Area in the following ways:

(a) By eliminating actual and potential competition between Genstar and Flintkote in the manufacture and sale of gypsum wallboard;

(b) Actual and potential competition among competitors generally in the manufacture and sale of gypsum wallboard may be lessened;

(c) The previously existing level of concentration in the manufacture and sale of gypsum wallboard in the 4-State Area will be increased and the possibilities of eventual deconcentration may be diminished.

VIII.

VIOLATION

32. Genstar's acquisition of 21.5% of the Common Stock of Flintkote constitutes a violation of Section 7 of the Clayton Act (15 U.S.C. 18) and Section 5 of the Federal Trade Commission Act (15 U.S.C. 45).

Decision and Order

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the New York Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act and the Clayton Act; and

The respondent, its attorney, and counsel for the Commission having hereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Acts, and that complaint should be issued stating its charges in that respect, and having thereupon accepted

the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, and having duly considered the comments filed thereafter by interested persons pursuant to Section 2.34 of its Rules and the recommendations of its staff, and respondent having consented by letter from its counsel, dated September 29, 1980, to a modification of the agreement containing consent order dated November 27, 1979, and the Commission having considered and accepted said modification, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. Respondent Genstar Limited is a corporation organized, existing and doing business under and by virtue of the laws of Canada, with its office and principal place of business located at One Place Ville Marie, Montreal, Quebec, Canada.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

ORDER

For purposes of this order, each of the following terms shall have the meaning ascribed thereto below:

A *cement-equivalent short ton* means: (i) in the case of finished cement, one short ton (2,000 pounds) and (ii) in the case of clinker, the product obtained by multiplying one short ton times 1.05.

Cement Facility means a cement manufacturing plant or a cement terminal, as the case may be, located in the States of Washington, Oregon, California or Nevada, and owned at the time by Flintkote or Genstar.

Cement Market Area means (i) the area included within the States of Washington, Oregon, California and Nevada or (ii) the area in the United States within a 300-mile radius of the cement manufacturing plant presently owned by Flintkote and located at Kosmosdale in Kentucky or (iii) the area in the United States within a 300-mile radius of the cement manufacturing plant presently owned by Flintkote and located at Glens Falls in New York, as the case may be, but in each case only for so long as there is located in that area a Product manufacturing plant owned by Genstar.

Dedicated Product for a particular calendar year means that quantity of Product manufactured at the Tilbury Plant by which (i) the total quantity of Product actually produced at the Tilbury Plant

during that year exceeds (ii) the quantity of Product so produced during that year and sold to buyers located in Canada except that the total quantity of Product actually produced at the Tilbury Plant in any year for purposes of this definition shall in no event exceed 982,000 cement-equivalent short tons.

Flintkote means The Flintkote Company, a Massachusetts corporation, its subsidiaries and affiliates.

Genstar means Genstar Limited and those persons, partnerships, subsidiary or related corporations or other legal entities acting on its behalf, their successors and assigns, including but not limited to Dorster, Inc.

Gypsum Market Area means (i) the area included within the States of Washington, Oregon, California and Nevada or (ii) the area in the United States within a 300-mile radius of the gypsum wallboard manufacturing plant presently owned by Flintkote and located at Florence in Colorado or (iii) the area in the United States within a 300-mile radius of the gypsum wallboard manufacturing plant presently owned by Flintkote and located at Sweetwater in Texas or (iv) the area in the United States within a 300-mile radius of the gypsum wallboard manufacturing plant presently owned by Flintkote and located at Savannah in Georgia or (v) the area in the United States within a 300-mile radius of the gypsum wallboard manufacturing plant presently owned by Flintkote and located at Camden in New Jersey, as the case may be, but in each case only for so long as there is located in that area a gypsum wallboard manufacturing plant owned by Genstar.

Independent Buyer means a company other than Flintkote or Genstar which owns a cement manufacturing plant or a cement terminal located in Washington, Oregon or California.

Product means finished portland cement or clinker, as the case may be.

Tilbury Plant means the cement manufacturing plant located at Tilbury Island, British Columbia, for so long as the same is owned by Genstar.

Independent Manufacturer means a company which is engaged in the manufacture and sale of Product in competition in the United States with Flintkote or Genstar.

I.

It is ordered, That respondent Genstar, a Canadian corporation, through its officers, directors, agents, representatives, employees, successors and assigns, directly or through any corporation, subsid-

iary, division or other device, in connection with the manufacture and sale of Product shall forthwith until January 31, 2000, cease and desist from establishing, entering into, continuing, carrying out, enforcing or cooperating or acquiescing in any contract, agreement, combination, understanding, arrangement or common course of action, whether express or implied, with any Independent Manufacturer doing business in the United States which has the effect of:

1. Respondent Genstar sharing in the profit realized by any Independent Manufacturer from the resale in the United States of Product purchased from Genstar.
2. Providing for the price of Product sold by respondent Genstar to any Independent Manufacturer to vary in relation to the selling price or margin or net realization of the Independent Manufacturer on its resale in the United States of said Product.
3. Respondent Genstar furnishing to, or receiving from any Independent Manufacturer to which respondent Genstar has sold or contracted to sell Product any information pertaining to:

(a) the cost of production of Product or sale of Product or any component thereof for either party;
(b) the sale price or the price realized by the Independent Manufacturer from the resale in the United States of Product purchased from Genstar.

II.

It is further ordered, That during the period commencing on the date this order becomes final and ending on January 31, 1990, respondent Genstar shall not, without the prior approval of the Federal Trade Commission, directly or indirectly sell or otherwise transfer or deliver to any Cement Facility for further processing or for resale any Product made by Genstar at any Product manufacturing plant located outside the United States and owned at the time by Genstar.

III.

It is further ordered, That for each calendar year during the period commencing on January 1, 1981 and ending on December 31, 1984, and for so much of the year 1980 as this order may be in effect, Genstar shall make available for sale to one or more Independent Buyers the Dedicated Product for that calendar year for delivery F.O.B. Genstar's Tilbury Plant during that year at a reasonable

market price (as determined during the relevant Offering Period described below) in accordance with the following procedures:

A. Except for the year 1980, Genstar shall, during or before the four (4) months immediately preceding such calendar year (which four (4) months shall be called the "Offering Period" for that calendar year), solicit orders at a reasonable market price from one or more Independent Buyers for delivery during that calendar year of all of the projected Dedicated Product for that year.

B. Except for the year 1980, to the extent that Genstar shall not, by November 1 during the Offering Period, have agreed to sell all of the projected Dedicated Product for that calendar year to Independent Buyers, Genstar shall within ten (10) business days thereafter notify each Independent Buyer in writing that Genstar is offering to sell, subject to prior agreements to sell to others, all or any portion of the then uncommitted Dedicated Product for that year for delivery during that year at a reasonable market price.

C. An Independent Buyer wishing to purchase any Dedicated Product offered pursuant to B. above shall submit to Genstar either a written acceptance of Genstar's offer or a written offer expressing the Independent Buyer's willingness to purchase during that year a specified quantity of such Dedicated Product at a specified price. Any such acceptance or offer must be submitted by December 1 during the Offering Period. Genstar shall enter into final agreements seriatim to sell to one or more of those Independent Buyers at a reasonable market price all Dedicated Product so offered for which Genstar received either such acceptances or such offers to buy at a reasonable market price. Genstar shall not in any event be obligated to enter into any agreement with any Independent Buyer to sell more Dedicated Product in a particular year than the portion thereof which Genstar has not committed to sell to others at the time at which the agreement to sell under this provision C. is entered into with that Independent Buyer.

D. Genstar shall be in complete compliance with the provisions of this Part III for 1980 if Genstar in fact sells to one or more Independent Buyers all of the Dedicated Product produced during that period of the year when this order may be in effect.

IV.

It is further ordered, That, for so long as the contract or contracts described below remain in force and effect, the provisions of Part III of this order shall be of no force or effect whatsoever if Genstar and

one or more Independent Buyers execute supply contracts pursuant to which Genstar shall become obligated to deliver F.O.B. the Tilbury Plant Product manufactured at the Tilbury Plant to such buyer or buyers, as the case may be, in amounts not less than 200,000 cement-equivalent short tons for 1980 and 300,000 cement-equivalent short tons for each of 1981, 1982, 1983 and 1984 provided that no such supply contract contains any terms (i) which provide for one party to furnish to the other data regarding either party's costs of production or sale, or profits on sales, of Product or (ii) which provide for the price of Product sold by Genstar to such buyer to vary in relation to the selling price or margin or net realization of the buyer with respect to resales of that Product or (iii) entitle Genstar to comply with the terms of such contract by supplying Product from any Cement Facility. Such a supply contract shall satisfy the requirements of this Part IV notwithstanding the fact that Genstar's obligation to supply under the contract may be subject to (i) force majeure, (ii) rights to reduce the quantity to be purchased which are exercisable by the Independent Buyer, and (iii) rights of Genstar to prorate Product among its customers if cement and clinker manufactured by it are short of the quantities required to supply its customers' requirements.

V.

It is further ordered, That respondent Genstar maintain adequate records, to be furnished upon request of the staff of the Federal Trade Commission, which evidence compliance with the provisions of this order, including, but not limited to records showing: the total quantity of product produced at the Tilbury Plant in the calendar year 1979 and each subsequent year for five (5) years up to and including the year 1984; the total quantity of Product so produced during each such year that was sold to buyers in Canada including the names and addresses of said buyers; copies of notices mailed to Independent Buyers in the United States soliciting orders for the Dedicated Product; copies of acceptances and sales agreements with said Independent Buyers and the names, addresses and the amount of Product purchased by each Independent Buyer in the United States.

VI.

It is further ordered, That Genstar's obligations under this order shall terminate if the following two conditions are met: (i) Genstar shall not prior to October 31, 1980 purchase any additional voting

securities issued by Flintkote and (ii) Genstar shall have divested prior to October 31, 1980 all interests it presently holds, directly or indirectly, in voting securities issued by Flintkote.

VII.

It is further ordered, That prior to January 31, 1985 Genstar shall cease and desist from acquiring, directly or indirectly, without the prior approval of the Federal Trade Commission, the whole or any part of:

A. any equity securities in excess of three (3) percent of the outstanding shares of such securities issued by any company, corporation or partnership which is engaged in either (i) the manufacture of Product in any Cement Market Area or (ii) the manufacture of gypsum wallboard in any Gypsum Market Area; or

B. any Product manufacturing plant or distribution terminal located in any Cement Market Area other than a Product distribution terminal which has not been used as such for at least three (3) months immediately preceding such acquisition; or

C. any gypsum wallboard manufacturing plant located in any Gypsum Market Area.

VIII.

It is further ordered, That Genstar, within sixty (60) days after service upon it of this order, file with the Federal Trade Commission a report, in writing, setting forth in detail the manner and form in which it has complied with this order.

IX.

It is further ordered, That respondent Genstar notify the Commission at least thirty (30) days prior to any proposed change in the respondent Genstar such as dissolution, assignment or sale resulting in the emergence of a successor corporation, or any other such change in the corporation which may affect compliance obligations arising out of the order.

Commissioner Pitofsky did not participate.

IN THE MATTER OF

AMERICAN ART CLAY CO., INC.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT

Docket C-3050. Complaint, Nov. 12, 1980—Decision, Nov. 12, 1980

This consent order requires, among other things, an Indianapolis, Ind. manufacturer of art materials to cease fixing the prices of its products. The firm is required to establish an interest-bearing escrow account for the purpose of making restitution to consumers for purchases of certain school art materials. Further, the firm is required to distribute consumer redress funds to any state institutions which purchased said products; the FTC, with the cooperation of the State Attorneys General, will distribute the respective funds in lump-sum amounts to each of the states which satisfy the application requirements for receiving the money.

Appearances

For the Commission: *Suzan L. Belman.*

For the respondent: *Joseph W. Burns, Lovejoy, Wasson, Lundgren & Ashton,* New York City.

COMPLAINT

The Federal Trade Commission, having reason to believe that the above-named respondent has violated the Federal Trade Commission Act, and that a proceeding by it in respect thereof would be in the public interest, issues this complaint.

Respondents

1. Respondent American Art Clay Co., Inc. is an Indiana corporation, with its principal office located at 4717 West 16th St., Indianapolis, Indiana.

2. At all times relevant to this complaint, respondent has been engaged in the manufacture, offering for sale, sale, and distribution of chalks, crayons, watercolors, or tempera paints.

Commerce

3. Respondent maintains, and has maintained, a substantial course of business, including the acts and practices alleged in this complaint, in or affecting commerce, as "commerce" is defined in Section 4 of the Federal Trade Commission Act, *as amended.*

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Competition

4. In the course and conduct of its business, and at all times mentioned herein, respondent has been in competition with other corporations, firms, or individuals engaged in the manufacture, offering for sale, sale, and distribution of chalks, crayons, watercolors, or tempera paints, except to the extent that competition has been restrained by the acts and practices alleged in this complaint.

Nature of the Offense

5. In the course and conduct of its business, respondent has engaged, or is engaging, in the following acts or practices, among others:

(a) For some years from at least as early as 1972, respondent and competitors engaged in the manufacture and sale of chalks, crayons, watercolors, or tempera paints, met, discussed and exchanged, prior to the publication of price lists for the forthcoming year, certain prices for those products, which were to be contained in such price lists.

(b) Through the meetings, discussions, and exchanges alleged in paragraph 5(a), respondent and competitors engaged in the manufacture and sale of chalks, crayons, watercolors, or tempera paints reached understandings or agreements concerning certain prices for those products to be contained in the published price lists for the forthcoming year.

(c) For some years from at least as early as 1972, respondent and competitors engaged in the manufacture and sale of chalks, crayons, watercolors, or tempera paints published and had in effect price lists which reflected a uniformity of retail prices for certain, if not all, chalks, crayons, watercolors, or tempera paints. The price lists usually were in effect for one year, and were used to establish uniform prices for sales to distributors and other customers.

(d) The price lists alleged in paragraph 5(c) reflected the understandings or agreements alleged in paragraph 5(b).

6. By means of certain, if not all, the acts and practices alleged in paragraph 5, among others, respondent, in combination, agreement, understanding, or conspiracy with others, has fixed or is fixing the prices at which certain, if not all, chalks, crayons, watercolors, or tempera paints were or are sold.

Thus, respondent has engaged, or is engaging, in unfair acts or

practices in violation of Section 5(a)(1) of the Federal Trade Commission Act.

Effects

7. The capacity, tendency or effect of the above conduct of respondent was to:

(a) Fix, control, establish, stabilize, or maintain the prices at which various of respondent's chalks, crayons, watercolors, or tempera paints are sold or resold.

(b) Lessen, eliminate, frustrate or hinder actual or potential competition in the sale and distribution of various of respondent's chalks, crayons, watercolors, or tempera paints.

(c) Artificially inflate the price paid by consumers for various of respondent's chalks, crayons, watercolors, or tempera paints.

(d) Deprive consumers of prices determined by free and open competition and of the other benefits of competition.

8. The acts and practices of respondent alleged here constitute unfair acts or practices in violation of Section 5(a)(1) of the Federal Trade Commission Act.

Decision and Order

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the Cleveland Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with a violation of the Federal Trade Commission Act; and

The respondent, and its attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order dated April 17, 1980 and modified as of September 12, 1980, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its

charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, and having duly considered the comments filed thereafter by interested persons pursuant to Section 2.34 of its Rules, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. Respondent American Art Clay Co., Inc. is an Indiana corporation, with its principal office located at 4717 West 16th St. in the City of Indianapolis, State of Indiana.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

ORDER

As used in this order:

(a) *Person* means any individual, partnership, firm, corporation, association, or other business or other legal entity.

(b) *State* means a state, the District of Columbia, Puerto Rico, the Virgin Islands, Guam, American Samoa, the Northern Mariana Islands, and any other territory of the United States.

(c) *State Institution* means any state agency, instrumentality, or institution or any political subdivision thereof, including, but not limited to, any county, city, town, municipality, or school district which purchases school art materials.

(d) *Art materials* means any of the following products: adhesives (including art and craft glue and white paste), art kits (including combinations of crayons, watercolors, brushes, glue or chalk), brushes, chalks (including art, chalkboard and industrial chalk), craft kits (including fabric crayons and fabric crayon kits), crayons (including drawing, checking, and marking crayons), modeling clays, oil pastels, paints (including finger paint, finger paint powder, tempera, poster paint, watercolors, and transparent, powder, and textile paints), paper (including finger paint paper and stencil paper), water color markers, stencil brushes, chalkboard cleaner, stencil knives, pencils (including drawing and charcoal pencils), modeling material, excello squares, ink (including printing ink), linoleum blocks, linoleum, acrylics, and media mixer.

(e) *Respondent* means American Art Clay Co., Inc., an Indiana

corporation, its subsidiaries and divisions, with its principal office located at 4717 West 16th St., Indianapolis, Indiana.

I

It is ordered, That respondent, its successors and assigns, and its officers, and respondent's agents, representatives, and employees, directly or indirectly, or through any corporation, subsidiary, division or other device, in connection with the manufacture, offering for sale, sale or distribution of art materials in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from directly or indirectly:

(1) Entering into, maintaining, or enforcing any agreement, combination, understanding or plan with any competitor to fix, determine, establish, or maintain the prices, discounts or other terms or conditions for the sale of art materials.

(2) Submitting any bid to any customer or prospective customer for the sale of any art materials when any price, term or condition of sale or any element contained in such bid was discussed with, disclosed to, or received from, directly or indirectly, any competitor, actual or potential.

(3) Circulating or sending to, or exchanging with, any other person who manufactures, distributes, markets or sells art materials, any price list, price quotation or pricing factor applicable to art materials—except for price lists, price quotations, or pricing factors provided to or received from any person in the course of, and solely related to, negotiating for, entering into, or carrying out bona fide sales or potential sales by respondent directly to such person—in advance of the printing, publication, effectuation, circulation or communication of such price lists, price quotations, or pricing factors to customers generally.

(4) Collecting from, circulating to or exchanging with, or reporting or recommending to any competitor who manufactures, distributes, markets or sells art materials, any cost factor or average cost of manufacture or sale of art materials, or any formulas for computing such cost.

(5) Communicating or exchanging with any other person who manufactures, distributes, markets, or sells art materials, any actual or proposed price, price change, discount, or other term or condition of sale at or upon which art materials are to be, or have been, sold—except for such information provided to or received from any person in the course of, and solely related to, negotiating for, entering into, or carrying out bona fide sales or potential sales by respondent

directly to such person—prior to the communication of such information to customers generally.

(6) Disclosing to, or communicating to, any other person who manufactures, distributes, markets, or sells art materials:

(a) respondent's intention to submit, or not to submit, a bid to any purchaser,

(b) the fact that a bid has or has not been submitted prior to the communication of such information to the general public, or

(c) the content of any bid prior to the communication of such information to the general public;

except that, in declining to furnish a price quotation to a distributor to be used in connection with a particular bid, respondent may disclose that the reason for such refusal is respondent's intention to bid directly.

II

It is further ordered, That respondent shall, for a period of five (5) years from the date of entry of this order, furnish simultaneously with each bid or quotation required to be sealed which is submitted by it for the sale of art materials to any purchaser, a written certification by an officer of respondent, that such bid was not in any way the result, directly or indirectly, of any agreement, understanding, or communication with any other producer, seller or distributor.

III

It is further ordered, That, for a period of five (5) years from the date of entry of this order, respondent shall preserve all written price computations and other written calculations actually performed by respondent in the preparation and submission of any bid required to be sealed which is submitted to any actual or potential purchaser of art materials. Respondent shall retain such written computations and calculations for a period of at least five (5) years from the date each bid which is based on such computations or calculations is submitted to any purchaser.

IV

It is further ordered, That:

(1) Prior to the fifth day after the date this order is served on respondent, the respondent shall establish an Escrow Account at the

Continental Bank, 30 North LaSalle St., Chicago, Illinois, and shall designate Continental Bank as the Escrow Agent to receive monies, information and documents, to disburse monies and to carry out such other functions as may be provided for pursuant to the terms of this order, and the written directions of the Federal Trade Commission or its designee. The duties of the Escrow Agent shall be as outlined in the Escrow Instructions here attached as Appendix A and incorporated herein. Further, the parties shall be bound to the terms of said Escrow Instructions whether or not they are signatories thereto.

(2) Respondent shall deposit twenty-five thousand dollars ($25,000) in the Escrow Account in the following manner. A first deposit of ten thousand dollars ($10,000) shall be made prior to the fifth day after the order is served on respondent, a second deposit of seven thousand, five hundred dollars ($7,500) shall be made on or before the first annual anniversary of the date of the first deposit, and the third and final deposit of the remaining seven thousand, five hundred dollars ($7,500) shall be made on or before the second annual anniversary of the date of the first deposit.

(3) All interest earned on the funds deposited in the Escrow Account shall be added to the Escrow Account and disbursed by the Escrow Agent pursuant to the terms of this order, the Escrow Instructions, and the written directions of the Federal Trade Commission or its designee.

(4) Respondent shall not issue any instructions or directions respecting the Escrow Account to the Federal Trade Commission or its designee, or to the Escrow Agent with respect to the performance of their duties. These duties shall be pursuant to this order and to the Escrow Instructions, and shall include, but not be limited to, the investment of the property held by the Escrow Agent, the disbursement of the property held by the Escrow Agent, and compliance with any written directions of the Federal Trade Commission or its designee. Respondent shall not exercise any control over the property in the Escrow Account.

V

It is further ordered, That:

(1) Respondent shall submit to the Federal Trade Commission, within thirty (30) days after the date this order is served on respondent, a notarized affidavit executed by a duly authorized officer of respondent listing, to the best of its knowledge, the names of all the states within which any state institutions made purchases

of respondent's chalk, crayons, watercolors, or tempera paints during any of the years 1972 through 1979, inclusive.

(2) As it has been determined by the Federal Trade Commission that the most readily identifiable and most significantly affected market consists of the school art materials purchasers, the sole purpose of the Escrow Account established pursuant to Section IV of this order is to disburse the consumer redress funds to any state institutions that purchase chalks, crayons, watercolors, or tempera paints for schools and are located in a state listed pursuant to Section V(1) of this order. Provisions contained herein or to be adopted in the future for the distribution of the funds are and shall be designed to accomplish such purpose in a manner most feasible, efficient and not inconsistent with the other provisions of this order.

(3) The Federal Trade Commission or its designee shall determine the appropriate recipients of funds in the Escrow Account, the sum paid to each recipient, and the most appropriate method to distribute the funds, taking into consideration the amount of funds available, the administrative feasibility and costs of disbursement, and the purpose of the Escrow Account, and shall instruct the Escrow Agent to distribute the funds in accordance with its determination.

(4) Funds to be distributed pursuant to paragraphs (1) through (3) of Section V of this order shall be paid out of the Escrow Account within three (3) years after the date of service of this order. All funds remaining in the Escrow Account after three (3) years from the date of service of this order shall be returned to respondent.

VI

It is further ordered, That respondent:

(1) Serve within sixty (60) days after the entry of this order a copy of this order upon each of its officers and directors, and upon each of its employees and agents who have any responsibility for establishing prices, discounts or other terms or conditions for the sale of art materials.

(2) File with the Federal Trade Commission three (3) separate written reports setting forth in detail the manner and form in which they have complied with this order; the first report to be filed within sixty (60) days after service upon them of this order, the second report to be filed within thirty (30) days after the first annual anniversary of the date of the first deposit, and the third report to be filed within thirty (30) days after the second annual anniversary of the date of the first deposit.

(3) Notify the Commission at least thirty (30) days prior to any

proposed change in the respondent which may affect compliance obligations arising out of this order.

APPENDIX A

To: Continental Illinois National Bank
and Trust Company of Chicago
Trust and Investment Services
Corporate Trust Division, Escrow Section
30 North LaSalle Street—10th Floor
Chicago, Illinois 60693

The following property will be deposited with you by the undersigned within the designated times:

An initial deposit of ten thousand dollars ($10,000) will be made at the time this account is established. Two additional deposits, each of seven thousand, five hundred dollars ($7,500), will be deposited in accordance with the instructions designated in paragraph 2 of section IV of the Agreement Containing Consent Order to Cease and Desist entered into between American Art Clay Company, Inc. and staff of the Cleveland Regional Office of the Federal Trade Commission, dated _____, 1980.

As Escrowee, you are hereby directed to hold, deal with and dispose of the aforesaid property and any other property at any time held by you hereunder in the following manner subject, however, to the terms and conditions hereinafter set forth:

A. In the event you are notified in writing by the Federal Trade Commission (hereinafter called the "FTC") or its designee that it has accepted the Agreement Containing Consent Order to Cease and Desist entered into between American Art Clay Company, Inc. (hereinafter called the "Company") and the staff of the Cleveland Regional Office of the Federal Trade Commission, dated April 17, 1980, and that the FTC has issued a Decision and Order in the Matter of American Art Clay Company, Inc., a corporation, you will hold the property and any other property at any time held by you hereunder (hereinafter called the "Property") until directed in writing by the FTC or its designee to distribute the Property, in which event the Property shall be distributed in accordance with its instructions.

In addition to deducting such fees, costs and expenses as incurred by you under paragraphs 7 and 8 hereof, you also will pay from the Property, as directed in writing by the FTC or its designee, such sums as you are authorized by the FTC or its designee to pay for the administration of the distribution scheme established by the FTC or its designee pursuant to the Agreement Containing Consent Order to Cease and Desist and the Decision and Order.

In addition, you shall execute such contracts regarding administration and distribution of the Escrow Account as the FTC or its designee directs. Subject to this paragraph, this Escrow will terminate upon the disbursement of all the Property pursuant to the written direction of the FTC or its designee.

B. In the event the FTC or its designee notifies you that it has determined not to accept the Agreement Containing Consent Order to Cease and Desist and to issue a Decision and Order as provided in Paragraph A, this Escrow will terminate and the Property will be returned by you to the Company not later than ten days after receipt of written notice from the FTC or its designee that the Agreement was not accepted.

C. Upon receipt of the Property you will invest the proceeds in either certificates of deposit other than certificates of deposit of Escrowee, or obligations of the United States Government or its agencies, either of which will have maturity not exceeding six (6) months from date of purchase. You will invest the Property with the aim of securing principal, while maximizing interest income. In the exercise of your sound discretion, if you determine it necessary to sell any or all of the Property prior to maturity and invest the proceeds in either other certificates of deposit or obligations of the United States Government or its agencies, you may do so.

D. Upon maturity of any of the Property you will invest the proceeds in either additional certificates of deposit other than certificates of deposit of Escrowee, or obligations of the United States Government or its agencies, either of which will have maturity not exceeding six (6) months from date of purchase. You will invest the proceeds with the aim of securing principal, while maximizing interest income. In the exercise of your sound discretion, if you determine it necessary to sell any or all of the Property prior to maturity and invest the proceeds in either other certificates of deposit or obligations of the United States Government or its agencies, you may do so.

E. You will send the FTC or its designee, monthly cash and asset statements of this Escrow Account.

F. These Escrow Instructions may be amended any time by a document duly executed by the FTC or its designee entitled "Amendment to Escrow Instructions" to which you acknowledge receipt.

G. If the FTC decides to use a designee, you will not act pursuant to such designee's orders, until you receive a certified copy of the order of the FTC naming such designee.

Terms and Conditions

1. Your duties and responsibilities shall be limited to those expressly set forth in these Escrow Instructions, and you shall not be subject to, nor obliged to recognize, any other agreement between, or direction or instruction of, any or all of the parties hereto even though reference thereto may be made herein; *provided, however,* with your written consent, these Escrow Instructions may be amended at any time or times by an instrument in writing signed by the FTC or its designee.

2. You are authorized, in your sole discretion, to disregard any and all notices or instructions given by any of the undersigned or by any other person, firm or corporation, except only such notices or instructions as are hereinabove provided for and orders or process of any court entered or issued with or without jurisdiction. If any Property subject hereto is at any time attached, garnished, or levied upon under any court order or in case the payment, assignment, transfer, conveyance or delivery of any such Property shall be stayed or enjoined by any court order, or in case any order, judgment or decree shall be made or entered by any court affecting such Property or any part thereof, then and in any of such events you are authorized, in

your sole discretion, to rely upon and comply with any such order, writ, judgment or decree which you are advised by legal counsel of your own choosing is binding upon you; and if you comply with any such order, writ, judgment or decree you shall not be liable to any of the parties hereto or to any other person, firm or corporation by reason of such compliance even though such order, writ, judgment or decree may be subsequently reversed, modified, annulled, set aside or vacated.

3. You shall not be personally liable for any act taken or omitted hereunder if taken or omitted by you in good faith and in the exercise of your own best judgment. You shall also be fully protected in relying upon any written notice, demand, certificate or document which you in good faith believe to be genuine.

4. Unless otherwise specifically indicated herein you shall proceed as soon as practicable to collect any checks or other collection items at any time deposited hereunder. All such collection shall be subject to the usual collection agreement regarding items received by your commercial banking department for deposit or collection. You shall not be required or have a duty to notify anyone of any payment or maturity under the terms of any instrument deposited hereunder, nor to take any legal action to enforce payment of any check, note or security deposited hereunder. You shall have no liability to pay interest on any money deposited or received hereunder.

5. You shall not be responsible for the sufficiency or accuracy of the form, execution, validity or genuineness of documents or securities now or hereafter deposited hereunder, or of any endorsement thereon, or for any lack of endorsement thereon, or for any description therein, nor shall you be responsible or liable in any respect on account of the identity, authority or rights of the persons executing or delivering or purporting to execute or deliver any such document, security or endorsement or these Escrow Instructions.

6. Any notices which you are required or desire to give hereunder to the FTC or its designee shall be in writing and may be given by mailing the same to the address provided by the FTC or its designee by United States mail, postage prepaid. For all purposes hereof any notice so mailed shall be as effectual as though served upon the FTC or its designee to whom it was mailed at the time it is deposited in the United States mail by you whether or not the FTC or its designee thereafter actually receives such notice. Notices to you shall be in writing and shall not be deemed to be given until actually received by your trust department employee or officer who administers this Escrow. Whenever under the terms hereof the time for giving a notice or performing an act falls upon a Saturday, Sunday, or holiday, such time shall be extended to the next business day.

7. If you believe it to be reasonably necessary to consult with counsel concerning any of your duties in connection with this Escrow, or in case you become involved in litigation on account of being Escrowee hereunder or on account of having received Property subject hereto, then in either case, your costs, expenses, and reasonable attorney's fees shall be paid by you from the Property with the approval of the FTC or its designee.

8. You shall be paid a reasonable fee for your services and reimbursed for your costs and expenses hereunder by you from the Property in accordance with the fee schedule attached hereto as Appendices 1 and 2 and incorporated herein.

9. If your fees, costs, expenses, or reasonable attorney's fees provided for herein, are not promptly paid, you shall have the right to sell the Property held hereunder and reimburse yourself therefor from the proceeds of such sale or from the cash held hereunder.

10. It is understood that you reserve the right to resign as Escrowee at any time by giving written notice of your resignation, specifying the effective date thereof, to the FTC or its designee. Within 30 days after receiving the aforesaid notice, the FTC or its designee agrees to appoint a successor Escrowee to which you may distribute the Property then held hereunder, less your fees, costs and expenses. If a successor Escrowee has not been appointed and has not accepted such appointment by the end of the 30-day period, you may apply to a court of competent jurisdiction for the appointment of a successor Escrowee, and the costs, expenses and reasonable attorneys' fees which you incur in connection with such a proceeding shall be paid from the Property.

11. The Escrowee will have no liability if, in order to make the distribution, there is any loss of interest resulting from the liquidation of investments prior to their maturity.

12. The Escrowee shall have no responsibility for any taxes arising with regard to the Escrow Account. Such tax obligation, if any, shall be the responsibility of the recipients of the Property.

13. This Escrow Agreement shall be construed, enforced, and administered in accordance with the laws of the State of Illinois.

14. The undersigned Escrowee hereby acknowledges receipt of the Property described in the above Escrow Agreement and agrees to hold, deal with and dispose of said Property and other Property at any time held by it hereunder in accordance with the foregoing Escrow Agreement.

15. Executed this _____ day of _____, _____ at Chicago, Illinois.

Parties to Escrow	Addresses
_____	_____
_____	_____
_____	_____
_____	_____
_____	_____
_____	_____
_____	_____

_____

ATTEST:

Continental Illinois National Bank and Trust Company of Chicago, Escrowee

_____ By: _____

Trust Officer

Vice President

Executed in _____ Copies

APPENDIX 1

SCHEDULE OF FEES FOR SERVICES AS ESCROW AGENT

A. ADMINISTRATION FEES

The following rates are applicable for ordinary services in handling an escrow subject to a minimum acceptance fee of $250 and minimum annual charge of $250. The Acceptance Fee will be based on the initial value of the deposits at the opening of the account.

ACCEPTANCE FEE

$250 minimum on assets up to $50,000
$1.25 per $1,000 on next $300,000 valuation
$ .50 per $1,000 on next $350,000 valuation
$ .20 per $1,000 on next $1,000,000 valuation
$ .10 per $1,000 on excess above $1,700,000 valuation

ANNUAL ADMINISTRATIVE FEE

$250 minimum on assets up to $50,000
$1.25 per $1,000 on next $300,000 valuation
$ .50 per $1,000 on next $350,000 valuation
$ .20 per $1,000 on next $1,000,000 valuation
$ .10 per $1,000 on excess above $1,700,000 valuation

The Annual Administrative Fee will be based on the value of the assets in the account at the beginning of the fee period plus any deposits made through the fee billing period.

When our only current duties consist of holding life or casualty insurance policies, the minimum annual fee will be reduced to $150 until the occurrence of a casualty, at which time the regular schedule will apply to the insurance proceeds.

* * * * * * *

APPENDIX 2

B. OPERATING SERVICE FEES

When the escrow account requires the maintenance of participants' or claimants' records, the issuance of payments, and the preparation of tax forms, the following schedule applies:

1.) $2.50 per account per year (includes up to two distributions),
2.) $0.50 per check issued over two distributions.

When the escrow requires the investment of funds, a $50 charge will be made for each

purchase or sale transaction. A $35 charge will be made for any free deposit or delivery of assets (securities, deeds, insurance policies, etc.).

C. TERMINATION

There are no separate termination charges. Fees for the final billing period will be prorated to the date of termination; subject to a minimum of six months from the date of inception.

D. MISCELLANEOUS

The fees quoted in this schedule apply to services ordinarily rendered in administering an escrow account, and are subject to a reasonable adjustment if we are called upon to undertake unusual duties, responsibilities, procedures, or if the cost of doing business increases. The cost of all stationery and supplies, telephone, postage, printing, or other out-of-pocket expenses will be added to our regular service charges. In determining our general schedule of fees, we have taken into consideration the various incidental benefits occurring to us from the operation of accounts. These include temporary availability to the Trust Department of funds resulting from the retention of dividends or interest in accounts pending disbursement, the execution of securities transactions for accounts, and funds from other sources.

* * * * * * *

IN THE MATTER OF

WEST COAST CREDIT CORPORATION, d/b/a FIDELITY FINANCE CO., INC.

MODIFYING ORDER IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-2600. Order, Nov. 19, 1974—Modifying Order, Nov. 26, 1980

This order reopens the proceeding and modifies the cease and desist order issued on August 20, 1975, 40 FR 12258, 84 F.T.C. 1328, by deleting the third *It is further ordered* paragraph of the original order. This paragraph required that when the firm instituted suits in any superior court in Washington State, they attach to any summons served upon consumers a notice giving defendants an adequate explanation of what the summons meant and directions for avoiding default. Since the revised Washington Superior Court summons form now affords an adequate explanation, there no longer appears to be a need for this requirement.

ORDER REOPENING THE PROCEEDING AND MODIFYING DECISION AND ORDER

On November 19, 1974, the Federal Trade Commission issued a Decision and Order against West Coast Credit Corporation. West Coast Credit has since been acquired by Citicorp Washington Financial Center, Inc. ("Citicorp Washington"). It does business in Washington as both Citicorp Washington and Fidelity Finance. As successor to West Coast Credit, Citicorp Washington is bound by the terms of the order.

The order requires West Coast Credit to refrain from certain debt collection practices; among other things, the order requires West Coast Credit, whenever they cause consumers to be served with Washington Superior Court summons and complaints, to attach a clear explanation of what the summons means and how to avoid a default judgment.

The revised Washington Superior Court Rules summons form now appears to afford an adequate explanation to consumers, and obviates the need for the summons explanation forms required by the Commission. Due to this changed condition of fact, it appears to the Commission that it is in the public interest to reopen this proceeding and alter its order to delete the portion of the order requiring a summons explanation form.

On September 24, 1980 the Commission issued an order to show cause why the Commission should not reopen the proceedings and delete the third *It is further ordered* paragraph of the original order.

Respondent did not reply to the Show Cause Order and no comments were filed.

It is ordered, That the proceeding be reopened.

It is further ordered, That the decision and order issued on November 19, 1974 is modified by deleting the third *It is further ordered* paragraph of the order.

IN THE MATTER OF

COMMERCIAL SERVICES COMPANY, INC., ET AL.

MODIFYING ORDER IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-2717. Order, Aug. 20, 1975—Modifying Order, Nov. 26, 1980

This order reopens the proceeding and modifies the cease and desist order issued by the Commission on August 20, 1975, 40 FR 44312, 86 F.T.C. 467, by deleting the third *It is further ordered* paragraph of the original order which requires that when the firm institutes suits in any superior court in Washington State, they attach to any summons served upon consumers a notice giving defendants an adequate explanation of what the summons means and directions for avoiding default. This portion of the order appears to be unnecessary since the revised Washington Superior Court summons form now affords consumers an adequate explanation.

ORDER REOPENING THE PROCEEDING AND MODIFYING DECISION AND ORDER

On August 20, 1975, the Federal Trade Commission issued a Decision and Order against Commercial Services Company, Inc. and other related parties. The order requires respondents to refrain from certain debt collection practices; among other things, the order requires Commercial Services, whenever they cause consumers to be served with Washington Superior Court summons and complaints, to attach a clear explanation of what the summons means and how to avoid a default judgment.

The revised Washington Superior Court Rules summons form now appears to afford an adequate explanation to consumers, and obviates the need for the summons explanation forms required by the Commission. Due to this changed condition of fact, it appears to the Commission that it is in the public interest to reopen this proceeding and alter its order, to delete the portion of the order requiring a summons explanation form.

On September 24, 1980 the Commission issued an order to show cause why the Commission should not reopen the proceedings and delete the third *It is further ordered* paragraph of the original order. Respondents did not reply to the Show Cause Order and no comments were filed.

It is ordered, That the proceeding be reopened.

It is further ordered, That the decision and order issued on August 20, 1975 is modified by deleting the third *It is further ordered* paragraph of the order.

IN THE MATTER OF

FARNAM COMPANIES, INC., ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF SECTION 5 OF THE FEDERAL TRADE COMMISSION ACT

Docket C-3052. Complaint, Dec. 11, 1980—Decision, Dec. 11, 1980

This consent order requires, among other things, a Phoenix, Ariz. firm and its corporate officer, engaged in the manufacture, advertising, sale and distribution of pesticide products, to cease representing, through print and broadcast advertising or otherwise, that their pesticide products are absolutely or unqualifiedly safe, non-toxic or free of hazard to humans, pets, wildlife or the environment; or making any representation that is inconsistent or which detracts from the effectiveness of required warnings or directions for use set forth on pesticide product labels. The firm is further prohibited, for a period of three years, from disseminating advertising or promotional material which fails to include a warning statement as designated in the order.

Appearances

For the Commission: *Allen R. Franck.*

For the respondent: *Steven Feola, Smith & Feola,* Phoenix, Ariz.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, as amended, and by virtue of the authority vested in it by said Act, the Federal Trade Commission having reason to believe that Farnam Companies, Inc., a corporation, and Russell W. McCalley, individually and as an officer of said corporation, [hereinafter sometimes referred to as respondents] have violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. Respondent Farnam Companies, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Arizona, with its principal office and place of business located at 2230 East Magnolia St., Phoenix, Arizona.

Respondent Russell W. McCalley is an officer of the corporation. He directs and controls the acts and practices of said corporate respondent, including the acts and practices hereinafter set forth. His address is the same as that of said corporate respondent.

PAR. 2. Respondents have been, and are now, engaged in the offering for sale, sale and distribution of various pesticide products,

including a snail and slug pesticide designated as "Snail Jail," to distributors, jobbers and retailers for resale to the public, and to the public at retail. For the purpose of this complaint and the order attached, the term "pesticide product" refers to any substance or mixture of substances, including molluscacides, intended for preventing, destroying, repelling or mitigating "plant pests" as defined at 7 U.S.C. 150aa(c).

PAR. 3. In the course and conduct of their business, respondents now cause, and for some time in the past have caused, said snail and slug pesticide to be shipped from their warehousing facilities in Omaha, Nebraska to purchasers located in various other States throughout the United States, and maintain, and at all times mentioned herein did maintain, a substantial course of trade in said product in commerce, as "commerce" is defined in the Federal Trade Commission Act.

PAR. 4. Snail Jail pesticide is registered with the Environmental Protection Agency as required under the Federal Pesticide, Fungicide and Rodenticide Act, 7 U.S.C. 136, et seq., and as required by that Act, the following warning label appears on the package in which the product is sold:

WARNING: Use only as directed. Read entire label before using. This pesticide may be fatal to children and dogs or other pets if eaten. Keep children and pets out of treated area. May be fatal if swallowed. Do not take internally. Harmful dust. Avoid breathing dust and vapor. Avoid contact with skin, eyes, and clothing. Do not contaminate or store near feed or food stuffs. Wash after handling. Baits should be spread in such a way that children, pets or farm animals cannot reach them. Birds feeding in treated areas may be killed. Do not store in direct sunlight. Do not reuse empty container. Wrap container and put in trash collection.

PAR. 5. In the course and conduct of their business, respondents have disseminated or caused to be disseminated advertisements concerning pesticide products, including "Snail Jail," by means of printed advertisements in magazines and newspapers distributed through the mail and by means of advertisements transmitted by television stations located in various States of the United States, which had the purpose of inducing and which were likely to induce, directly or indirectly, the purchase of pesticide products, including "Snail Jail."

PAR. 6. Among the advertisements so disseminated or caused to be disseminated by respondents are those contained in Exhibits A through G, attached hereto and by this reference made a part hereof.

PAR. 7. The aforesaid advertisements represent directly or by implication that:

1. Snail Jail protects users, pets and children, is completely safe for children and is non-toxic.

2. Snail Jail's toxic ingredients [metaldehyde and carbaryl] are locked inside a plastic container and can not come in contact with skin no matter how much it is handled.

3. The Environmental Protection Agency has approved Snail Jail as safe for users, children, pets and the general environment.

PAR. 8. In truth and in fact:

1. Snail Jail is potentially harmful to users, pets and children who swallow or have contact with the toxic ingredients in the product.

2. Snail Jail's toxic ingredients can come into contact with skin through handling of the Snail Jail container.

3. The Environmental Protection Agency has not approved Snail Jail as safe for users, pets, children, or the general environment.

Therefore, the aforesaid advertisements were, and are, deceptive or unfair.

PAR. 9. By making statements and representations, alone or in cooperation with others, orally or in writing, which appear in advertisements in print or broadcast media, in promotional material and by other means, about Snail Jail in a manner which is inconsistent with or disregards warnings, cautions, limitations and instructions for use found in labeling, respondent negates the import and purposes of, and detracts from the effectiveness of such warnings, cautions, limitations or instructions.

Therefore, the advertisements and other promotional materials, which contain the statements and representations referred to in Paragraph Nine above are unfair or deceptive.

PAR. 10. In the further course and conduct of its business as aforesaid, respondents have made statements and representations, alone or in cooperation with others, orally or in writing, which appear in advertisements in print and broadcast media, in promotional material or by other means, about Snail Jail without disclosing that such products are hazardous. Knowledge of the hazards associated with the use of such products would enable and encourage consumers to exercise the proper degree of care in using them.

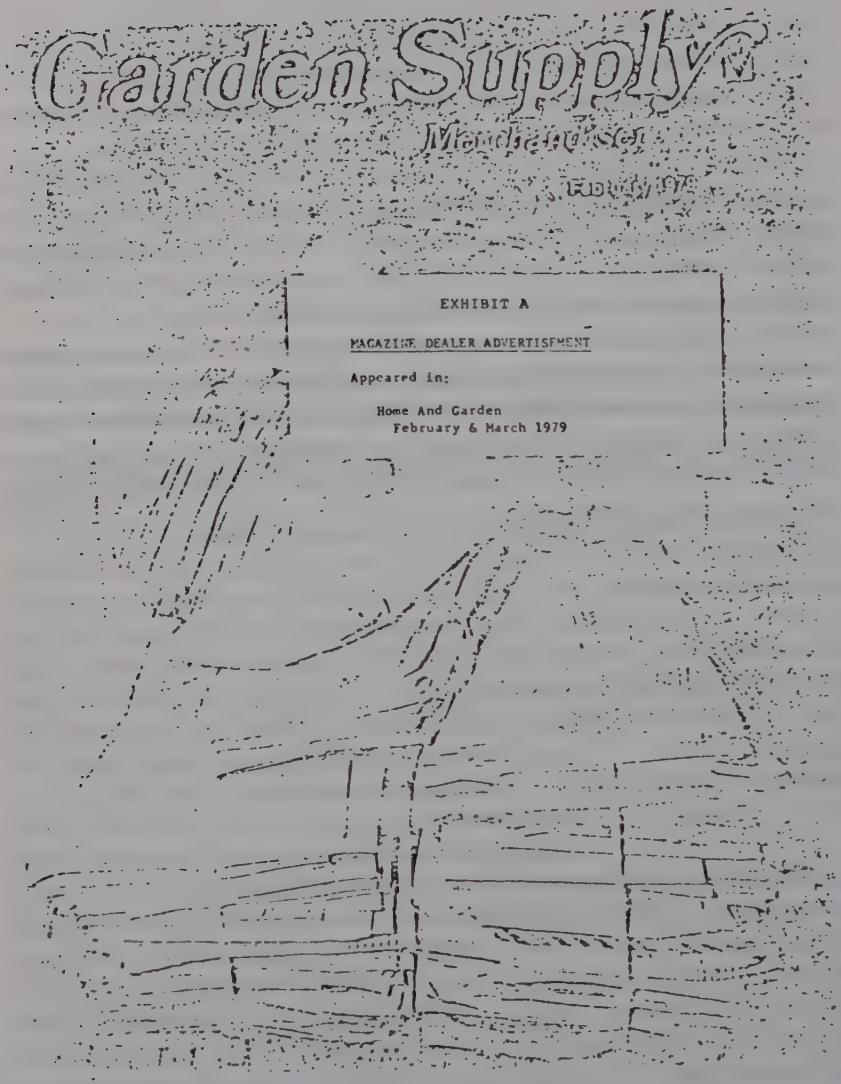
Thus, respondents have failed to disclose material facts which, if known to consumers, would be likely to affect their consideration of whether or not to purchase, and how to properly use, such products. Therefore, advertisements, promotional materials, acts and prac-

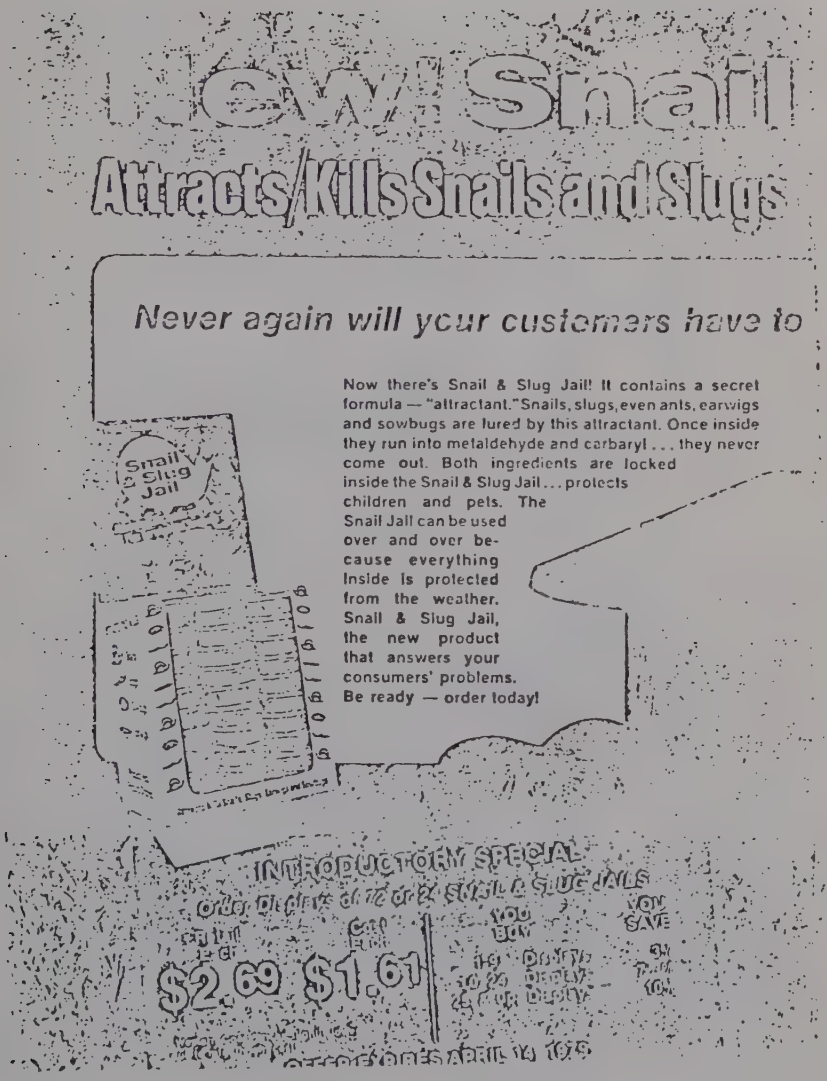
tices, which fail to disclose the aforesaid material facts, are unfair or deceptive.

PAR. 11. In the course and conduct of their business, and at all times mentioned herein, respondents have been and now are, in substantial competition, in or affecting commerce, with corporations, firms and individuals engaged in the sale of merchandise of the same general kind and nature as merchandise sold by respondents.

PAR. 12. The use by respondents of the aforesaid unfair or deceptive statements, representations, acts and practices directly or by implication, has had, and now has, the capacity and tendency to mislead members of the consuming public into the purchase of substantial quantities of respondents' pesticide products.

PAR. 13. The acts and practices of respondents, as herein alleged, were and are all to the prejudice and injury of the public and of respondents' competitors and constituted, and now constitute, unfair methods of competition and unfair or deceptive acts or practices in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act, as amended.


Garden Supply
EXHIBIT A
MAGAZINE DEALER ADVERTISEMENT
Appeared in:
Home And Garden
February & March 1979


New Snail
Attracts/Kills Snails and Slugs
Never again will your customers have to
Now there's Snail & Slug Jail! It contains a secret formula — "attractant." Snails, slugs, even ants, earwigs and sowbugs are lured by this attractant. Once inside they run into metaldehyde and carbaryl . . . they never come out. Both ingredients are locked inside the Snail & Slug Jail . . . protects children and pets. The Snail Jail can be used over and over because everything inside is protected from the weather. Snail & Slug Jail, the new product that answers your consumers' problems. Be ready — order today!
Snail & Slug Jail
INTRODUCTORY SPECIAL
$2.69 $1.61

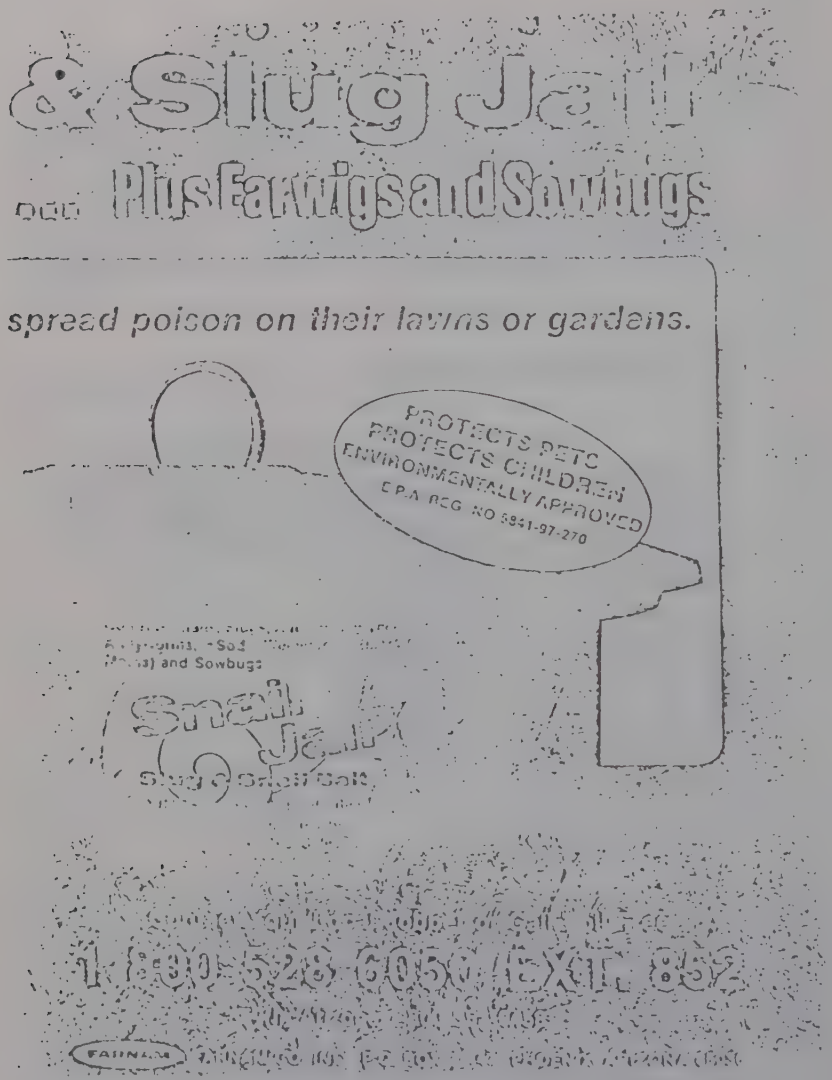

& Slug Jail
Plus Earwigs and Sowbugs
spread poison on their lawns or gardens.
PROTECTS PETS
PROTECTS CHILDREN
ENVIRONMENTALLY APPROVED
E.P.A. REG. NO 5841-97-270
and Sowbugs
Snail Jail
1-800-528-6050 EXT. 852
FARNAM

EXHIBIT B

NEWSPAPER AD

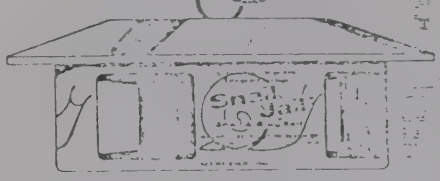
Appeared in:

Times Picayune
New Orleans, La.
7/13, 7/14, 7/15/79

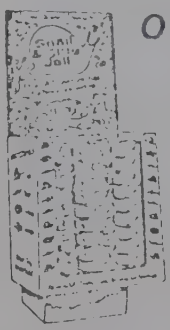
Dallas Morning News
Dallas, Texas
7/13/79

Attract and Kill Snails, Slugs, Pill Bugs, Earwigs With Amazing New!

Snail™ Jail



- Approved lure attracts and destroys garden pests without spreading harmful poison meal or pellets
- Designed to protect pets, children and garden wildlife
- Environmentally approved — EPA #5841-97-210
- Effective over a 500 square foot area
- Bait and chemicals locked inside — only snails, slugs, and bugs can reach it
- Convenient disposable container
- Can't come in contact with skin no matter how much it's handled
- Won't wash away in the rain, or blow away in the wind
- Reusable basis for weeks!



ONE LOW PRICE

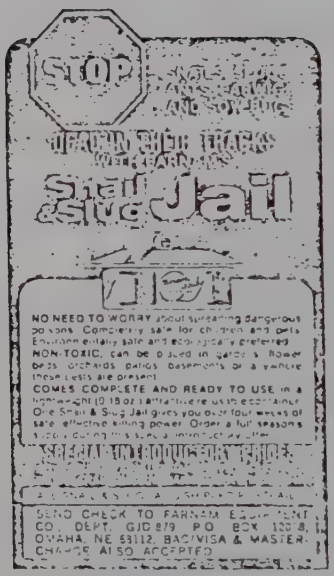
BUYS MONTHS OF PROTECTION FOR YOUR YARD, VEGETABLE GARDEN, & FLOWER GARDEN — THROUGH ALL TYPES OF WEATHER!

LOOK FOR THIS DISPLAY AT YOUR NEAREST FARNAM DEALER TODAY!

Snail Jail is available at the following stores in the Dallas area:

Turner Hardware
Handy Dan's *(all stores)*
Chuck's Nursery
Blalock Gardens
Gibson's *(selected stores)*
Skaggs *(all stores)*
Bruce Miller's Nursery
C & S Hardware Stores *(all stores)*
Stroud's Garden Center
Mr. G's Garden Center

EXHIBIT C



MAGAZINE ADVERTISEMENT

Appeared in:

Elks Magazine, April 1979
Family Food Garden, April 1979
Moose, April 1979
National Gardener, July 1979, August 1979
Organic Gardening, April 1979
Sunset Magazine, May 1979
VFW, April 1979

EXHIBIT D

STOP
Snail
Slug Jail
NO NEED TO WORRY about spreading dangerous poisons. Completely safe for children and pets. Environmentally safe and ecologically preferred.
NON-TOXIC, can be placed in gardens, flower beds, orchards, patios, basements or anywhere these pests are present.
THESE PESKY DEVILS do more damage to vegetables, flowers, citrus, shrubs, trees and lawns than any other living insect.
STOP THESE PESTS FOREVER with Farnam's new, unique Snail & Slug Jail. It attracts and kills these pests in one easy step.
COMES COMPLETE AND READY TO USE in a lightweight, plastic trap. Attract-release-recapture. One Snail & Slug Jail gives you over four years of safe, effective killing power. Order a full season's supply during this special introductory offer.
Farnam Equipment Co.

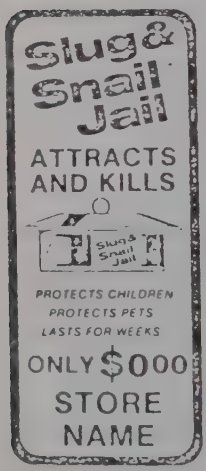
MAGAZINE ADVERTISEMENT

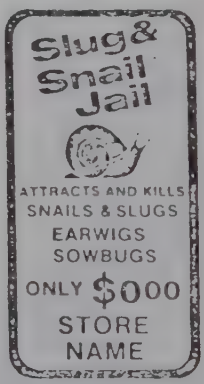
Appeared in:

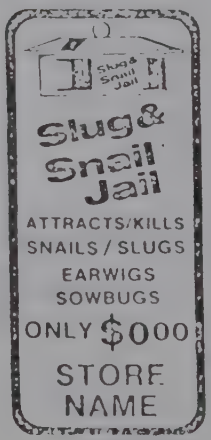
Family Handyman, April 1979
Flower & Garden, April 1979
Kiwanis, April 1979
Mechanix Illustrated, April 1979
Workbench, May 1979, June 1979
Progressive Farmer, April 1979

EXHIBIT E

ADVERTISING SLICK SENT TO DEALERS





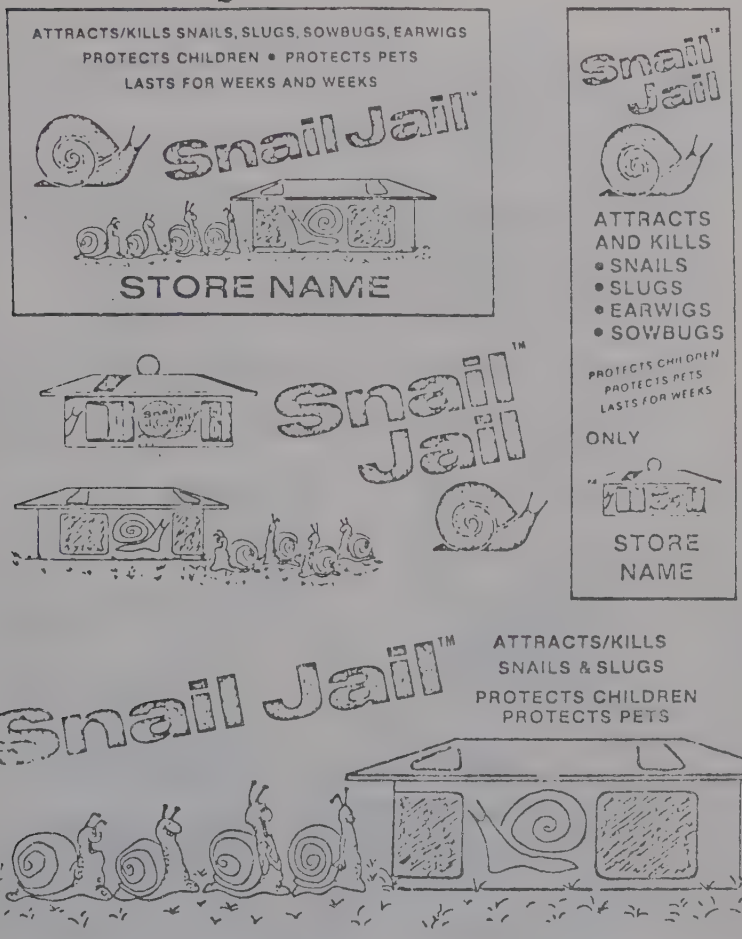


Slug& Snail Jail

© 1978 FARNAM COMPANIES, INC., OMAHA, NEBRASKA 68112.

EXHIBIT F

ADVERTISING SLICK SENT TO DEALERS



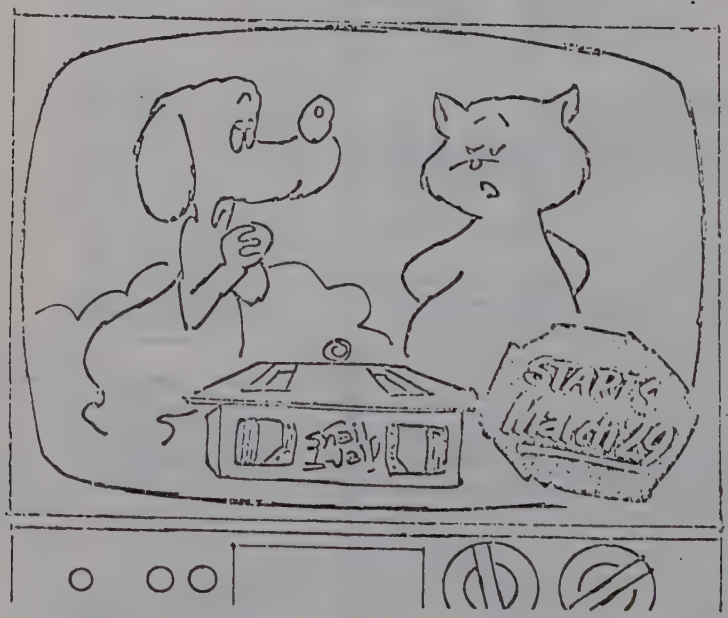
78 FARNAM COMPANIES, INC., OMAHA, NEBRASKA 68112

DEALER MAILER Story Board for Television Ads

EXHIBIT G

Introducing...

Your Two New SuperStomping Snail Jail Salesmen!



Dynamic, Fully Animated Tele
Commercial Starts Selling S
For You On March 29th!

LOS ANGELES...
SAN FRANCISCO...
SAN DIEGO...

8 WEEK SCHEDULE ON
NETWORK STATIONS

BEST TIMES!

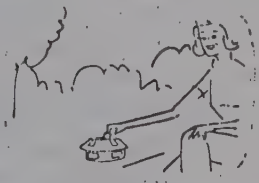
:30 SECOND
FULL-ANIMATION

OVER 1455
HOUSEHOLD
RATING POINTS

3.

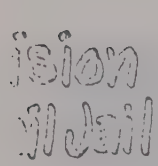
4.

7. (Voice Over) Snail Jell, it's totally new!



11. ...snails and slugs ... for up to 500 square feet.

12.



1. DOG "What Happened?"
CAT "Don't Cha Remember?"

2. CAT: "... We were in the back yard
havin' a picnic with all those
yummy tasain pellets!"

These ain't no doggy treats ...
re Snail pellets!"

5. DOG "Why didn't our master use Snail
Jail?"
CAT: "I'll mention it to him ..."

6. "... I've got eight lives to go!"

No poison to spread in your yard

9. Snail Jail's bait and chemicals are
locked inside ...

10. ... away from pets and kids. Snail Jail
attracts and kills ...

ills for weeks! (End Voice Over)

13. CAT: "In case your pet ..."

14. "... doesn't have nine lives"

Decision and Order

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondents named in the caption hereof, and the respondents having been furnished thereafter with a copy of a draft of complaint which the Denver Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondents with violation of the Federal Trade Commission Act; and

The respondents, their attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondents of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondents that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondents have violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent Farnam Companies, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Arizona, with its office and principal place of business located at 2230 East Magnolia St., Phoenix, Arizona.

Respondent Russell W. McCalley is an officer of said corporation. He formulates, directs and controls the policies, acts and practices of said corporation, and his principal office and place of business is located at the above-stated address.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents, and the proceeding is in the public interest.

Order

It is ordered, That Farnam Companies, Inc., a corporation, its successors and assigns, and its officers, and Russell W. McCalley, individually and as an officer of said corporation, and respondents'

336-345 O - 81 - 54

representatives, agents, and employees, directly or through any corporation, subsidiary, division or other device, in connection with the advertising, offering for sale, sale or distribution of pesticide products in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended, do forthwith cease and desist from:

1. Representing directly or by implication, by print or broadcast advertising, other promotional material, or through sales representatives' oral statements, that the pesticide products manufactured, distributed or sold by or through said respondents are absolutely or unqualifiedly safe, non-toxic or free of hazard to adults, children, pets, wildlife or the environment.

2. Making any representation, directly or by implication, by print or broadcast advertising or other promotional material, which contradicts, is inconsistent with, or detracts from the effectiveness of any warning, caution or direction for use required by law to be set forth as a label on pesticide products.

3. Representing that the Environmental Protection Agency or any other governmental agency had approved any pesticide product, unless such is the case; or misrepresenting the scope of approval granted any such product by any governmental agency.

It is further ordered, That for the period of three (3) years following the date of service of this order, respondents shall not disseminate or cause the dissemination of:

a) Any print advertising or print promotional material for any pesticide product unless the following statement is clearly and conspicuously included in such print advertising or print promotional material:

ALL PESTICIDES CAN BE HARMFUL TO HEALTH AND
THE ENVIRONMENT IF MISUSED. READ THE LABEL CAREFULLY
AND USE ONLY AS DIRECTED.

b) Any television broadcast advertisement for any pesticide product unless such advertisement orally and visually includes the following statement made in a clear and conspicuous manner:

ALL PESTICIDES CAN BE HARMFUL.
READ THE LABEL. USE AS DIRECTED.

c) Any other broadcast advertisement for any pesticide product unless such advertisement orally includes the following statement in a clear and conspicuous manner:

ALL PESTICIDES CAN BE HARMFUL.
READ THE LABEL. USE AS DIRECTED.

It is further ordered, That respondent, Farnam Companies, Inc., forthwith distribute a copy of this order to all its operating divisions engaged in the sale, advertising, promotion or distribution of pesticide products and to all present and future employees of said respondent responsible for the advertising, promotion, distribution or sale of such products, and that said respondents secure from each such person a signed statement acknowledging receipt of said order.

It is further ordered, That respondent, Farnam Companies, Inc., notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondent such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporation which may affect compliance obligations arising out of this order.

It is further ordered, That the individual respondent named herein promptly notify the Commission of the discontinuance of his present business or employment and of his affiliation with a new business or employment. In addition, for a period of ten (10) years from the date of service of this order, said respondent shall promptly notify the Commission of each affiliation with a new business or employment. Each such notice shall include the respondent's new business address and a statement of the nature of the business or employment in which the respondent is newly engaged as well as a description of respondent's duties and responsibilities in connection with the business or employment. The expiration of the notice provision of this paragraph shall not affect any other obligation arising under this order.

It is further ordered, That each of the respondents herein shall within sixty (60) days after service upon them of this order, file with the Commission a report, in writing, setting forth in detail the manner and form in which each has complied with this order.

It is further ordered, That this order shall become effective upon service.

IN THE MATTER OF

EQUIFAX INC.

FINAL ORDER, OPINION, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FAIR CREDIT REPORTING ACT AND SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT

Docket 8954. Complaint, Feb. 21, 1974—Final Order, Dec. 15, 1980

This order requires, among other things, an Atlanta, Ga. consumer credit reporting firm to cease misrepresenting the identity of its investigative personnel; improperly providing its customers with updated consumer report information; and rewarding or punishing its employees on the basis of the amount of adverse information collected and included in their reports on consumers. The order further requires that the company cease failing to make statutorily required disclosures to consumers requesting information concerning their credit status; provide such consumers with all the information in its files; and reinvestigate any disputed item of information promptly.

Appearances

For the Commission: *Robert W. Russell, Virginia M. Conway* and *David G. Grimes, Jr.*

For the respondent: *Willis B. Snell, Francis M. Gregory, Jr., Michael L. Denger* and *Shelley Zena Green, Sutherland, Asbill & Brennan,* Washington, D.C.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act and the Fair Credit Reporting Act, and by virtue of the authority vested in it by said Acts, the Federal Trade Commission, having reason to believe that Retail Credit Company, a corporation, hereinafter referred to as respondent, has violated the provisions of said Acts, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint, stating its charges in that respect as follows:

DEFINITIONS

PARAGRAPH 1. For the purpose of this Complaint the following definitions apply:

(a) "consumer reporting agency"—any person which, for monetary fees, dues, or on a cooperative nonprofit basis, regularly engages in whole or in part in the practice of assembling or evaluating

consumer credit information or other information on consumers for the purpose of furnishing consumer reports to third parties, and which uses any means or facility of interstate commerce for the purpose of preparing or furnishing consumer reports.

(b) "investigative personnel"—individuals, including, but not necessarily limited to, respondent's Field Inspectors, Field Representatives, Fee Inspectors and Claims Inspectors, engaged in the preparation of consumer reports and other reports.

(c) "consumer report"—any written, oral, or other communication of any information bearing on a consumer's credit worthiness, credit standing, credit capacity, character, general reputation, personal characteristics, or mode of living which is used or expected to be used or collected in whole or in part for the purpose of serving as a factor in establishing the consumer's eligibility for (1) credit or insurance to be used primarily for personal, family, or household purposes, (2) employment purposes, or (3) other purposes authorized under Section 604 of the Fair Credit Reporting Act.

(d) "investigative consumer report"—a consumer report or portion thereof in which information on a consumer's character, general reputation, personal characteristics, or mode of living is obtained through personal interviews with neighbors, friends, or associates of the consumer reported on or with others with whom he is acquainted or who may have knowledge concerning any such item of information.

(e) "claims report"—a report containing information prepared for an insurance company on an insured for the purpose of determining the validity of a claim for a benefit filed under an existing insurance policy and/or utilized in the negotiation of a settlement of said claim.

(f) "medical information"—information or records obtained directly or indirectly from licensed physicians or medical practitioners, hospitals, clinics, or other medical or medically related facilities.

(g) "adverse information"—negative or derogatory information which may have, or may reasonably be expected to have, an unfavorable bearing on a consumer's eligibility or qualification for a benefit such as insurance, including information which may result or which may reasonably be expected to result in a denial of or increased cost for such benefit.

PAR. 2. Respondent is a corporation, organized existing and doing business under and by virtue of the laws of the State of Georgia, with its principal office and place of business located at 1600 Peachtree St., N.W., Atlanta, Georgia.

PAR. 3. Respondent is a consumer reporting agency as defined herein, with approximately 300 branch offices and 1500 other offices

located in every State of the United States. Respondent, the nation's largest company in the consumer reporting industry, is engaged in the business of obtaining, maintaining and selling information about consumers to over 84,000 business customers. Respondent employs approximately 8500 investigative personnel who interview approximately 200,000 individuals daily and prepare about 35 million reports per year. Through its nationwide network of offices, respondent has the capacity to provide information on 98 percent of the population of the United States. Its revenues for 1972 are listed at 195 million dollars, resulting in gross income of over 17 million dollars.

PAR. 4. In the ordinary course and conduct of its business, as aforesaid, respondent causes and for some time in the past has caused reports, including consumer reports, investigative consumer reports and claims reports, as defined herein, to be distributed through the mail from its branch offices and other offices located in all fifty states and the District of Columbia, to its customers located in various other States of the United States.

Therefore, respondent maintains, and at all times mentioned herein has maintained, a substantial course of trade in the aforesaid products and services in commerce, as "commerce" is defined in the Federal Trade Commission Act.

COUNT I

Alleging violations of Section 5 of the Federal Trade Commission Act, the allegations of Paragraphs One through Four above, are incorporated by reference as if fully set forth herein verbatim:

PAR. 5. In the ordinary course and conduct of its business, as aforesaid, respondent, through its investigative personnel, prepares reports, including consumer reports, investigative consumer reports and claims reports, by interviewing the consumer and others telephonically or in person. In these interviews, respondent's investigative personnel, in certain instances, represent, directly or by implication, that:

1. they are agents or employees of the company to which the consumer has applied for a benefit, such as insurance; and/or
2. the information furnished by the consumer or others during an interview, will be used exclusively by the company to which the consumer has applied for a benefit, such as insurance.

PAR. 6. In truth and in fact:

1. respondent's investigative personnel are not agents or employees of the company to which the consumer has applied for a benefit; and/or

2. the information furnished by the consumer or others during an interview, will not be used exclusively by the company to which the consumer has applied for a benefit. The information is added to respondent's files for future reference in connection with any subsequent requests by other customers for reports on the consumer, who is the subject of the interview.

The practice by respondent's investigative personnel of failing to disclose both their identity and/or the full use to be made of the information obtained during the interviews, leads consumers and others into the false and mistaken belief that they are providing information directly to the agent or employee of a company which will use the information exclusively in determining the consumer's eligibility for a benefit. Some of those interviewed would have elected to provide information directly to said company rather than to respondent had the true identity of the interviewer, or the fact that the information obtained is to be added to respondent's files for future reference, been known.

Therefore, the representations set forth in Paragraph Five above, were and are unfair, false, misleading and deceptive in violation of Section 5 of the Federal Trade Commission Act.

PAR. 7. In the ordinary course and conduct of its business, as aforesaid, respondent's investigative personnel, in the preparation of certain reports such as claims reports, employ an interview technique whereby they interview consumers and others and represent, directly or by implication, that the investigation is for a specific purpose, such as a "routine credit check" or other similarly unrelated purpose.

PAR. 8. In truth and in fact, the purpose of the investigation is often other than as represented. For example, in certain instances, the purpose of the investigation is an evaluation of the consumer's claim for loss or injury under the terms of an existing insurance policy and the purpose of the interview is to observe the consumer's physical appearance, movements, or mental or physical capabilities. Such a claim for loss or injury is of high significance to the consumer. The use of the interview technique, as aforesaid, results in information being gathered under false pretenses.

Furthermore, information gathered in this way will be retained in respondent's files for possible use in reports for other customers.

Therefore, the practice set forth in Paragraph Seven above, was

and is unfair, false, misleading and deceptive in violation of Section 5 of the Federal Trade Commission Act.

PAR. 9. In the ordinary course and conduct of its business, as aforesaid, respondent, by and through its reports, its promotional literature and other means, represents, directly or by implication, to its customers, that its reports are compiled from information obtained through in-person interviews with the consumer who is the subject of the report, or his friends, neighbors, or associates; from direct observation of the consumer's home, neighborhood, or other physical surroundings; or through interviews with the "sources" indicated on the reports. Typical and illustrative of these representations, but not all inclusive thereof, are the following statements found in respondent's actual reports:

(1) the consumer presents a "healthy appearance with no ovious [sic] impairments or apparent tensions";

(2) the consumer's "residence seems small and inadequate"; and

(3) the consumer "had a white gauze bandage tacked over his eye to shield it from the light".

The representations as to the manner in which the information in the reports is gathered, i.e., through in-person interviews with the consumer who is the subject of the reports, or his friends, neighbors, or associates; from direct observation of the consumer's home, neighborhood, or other physical surroundings, or through interviews with the "sources" indicated on the reports, are relied upon by users, such as insurance companies, in evaluating the validity or accuracy of the information in the reports. Moreover, in certain instances, users rely upon the information in the reports to determine the consumer's eligibility for a benefit, such as insurance, or to increase the rate for, or to cancel the consumer's insurance coverage.

PAR. 10. In truth and in fact, in certain instances:

(1) the consumer who is the subject of the report, or the consumer's friends, neighbors or associates are interviewed only telephonically, rather than in person, as represented;

(2) the consumer's home, neighborhood or other physical surroundings are not observed directly as represented; and

(3) all "sources" listed on respondent's reports are not interviewed, as represented, either in person or telephonically.

Users would not give as much weight to or rely as heavily on the information in the reports in making a decision as to the consumer's eligibility for a benefit such as insurance had the manner in which

the reports were prepared been truthfully and factually represented. In fact, in certain instances, users would not reject a consumer's application for a benefit such as insurance or increase the rate for or cancel the consumer's insurance coverage, had the manner in which the information was gathered been truthfully and factually represented.

Therefore, the representations set forth in Paragraph Nine above, were and are unfair, false, misleading and deceptive in violation of Section 5 of the Federal Trade Commission Act.

PAR. 11. In the ordinary course and conduct of its business, as aforesaid, respondent obtains from insurance companies photocopies of statements signed by consumers authorizing the release of medical information to those insurance companies, but which are silent as to the release of said information to anyone else, including respondent. With these photocopies, respondent obtains medical information from consumers' doctors, clinics or other medical facilities, forwards the information to the named insurance companies, and retains a copy of such information in its files.

PAR. 12. In connection with the above practice, respondent represents, directly or by implication, to physicians or other medical personnel, that the information is being obtained for the exclusive use of the named insurance company to which the consumer executed the authorization. Moreover, consumers executing the authorizations for release of confidential medical information believe that the information will be obtained and used by the named insurance company exclusively.

PAR. 13. In truth and in fact, in certain instances, the information is not obtained for the exclusive use of the insurance company to which the consumer executed the authorization. A copy of the medical information is retained in respondent's files and has been, in certain instances, used in the preparation of subsequent reports for other customers. Some consumers would not have authorized the release of such confidential information had they known it would be obtained and utilized by a third party such as a consumer reporting agency.

Therefore, the acts and practices set forth in Paragraphs Eleven and Twelve above, were and are unfair, misleading and deceptive in violation of Section 5 of the Federal Trade Commission Act.

PAR. 14. The aforesaid acts and practices of respondent, as herein alleged, were and are all to the prejudice and injury of the public and of respondent's competitors and constituted, and now constitute, unfair methods of competition in commerce and unfair or deceptive

acts or practices in commerce in violation of Section 5 of the Federal Trade Commission Act.

COUNT II

Alleging violations of the Fair Credit Reporting Act and of the Federal Trade Commission Act, the allegations of Paragraphs One through Three are incorporated by reference as if fully set forth herein verbatim:

PAR. 15. Respondent in the ordinary course and conduct of its business as aforesaid is now, and subsequent to April 25, 1971 has been, engaged in the preparation, offering for sale, sale and distribution of information on consumers, including consumer reports and investigative consumer reports, as defined herein.

PAR. 16. In the ordinary course and conduct of its business, as aforesaid, respondent provides its customers what it terms a "Voluntary Follow-Up Service". Through this and other similar services, respondent, periodically and on an unsolicited basis, submits to customers such as insurance companies, adverse information about consumers upon whom previous consumer reports have been furnished. At the time said information is furnished, respondent has no reason to believe that it will be used in connection with a business transaction such as the underwriting of insurance. Rather, this additional information is submitted to customers to demonstrate the value or utility of respondent's reporting service.

PAR. 17. By and through the use of the aforesaid practice, respondent has furnished, and is furnishing, consumer reports and investigative consumer reports, as those terms are defined herein, to persons whom it has no reason to believe intend to use the information for one of the permissible purposes set out in Section 604 of the Fair Credit Reporting Act, and respondent thereby was and is in violation of that Section of the Act.

PAR. 18. In the ordinary course and conduct of its business, as aforesaid, respondent, in certain instances, reports to its customers the existence of items of adverse information, as defined herein, which antedate the consumer report by more than seven years. Typical and illustrative of the practice described herein, but not all inclusive thereof, are the following:

1. The inclusion of the following notice in some of its consumer reports:

In compliance with the Fair Credit Reporting Act no additional information can be

reported from this former employer covering employment experience prior to seven years ago.

2. The furnishing of photocopies of motor vehicle reports reflecting masked out or obliterated driving violations which antedate the report by more than seven years, but which indicate the existence of said obsolete violations.

PAR. 19. By and through the use of the aforesaid practices, respondent has reported and is reporting the existence of items of obsolete adverse information in violation of Section 605 of the Fair Credit Reporting Act.

PAR. 20. In the ordinary course and conduct of its business, as aforesaid, respondent employs certain procedures in the preparation of consumer reports and investigative consumer reports, as defined herein, which do not assure the maximum possible accuracy of the information concerning the individuals about whom the reports relate. Typical and illustrative of such procedures, but not all inclusive thereof, are the following:

(1) a salary/production system which requires or compels its investigative personnel, as defined herein, to complete or prepare an unreasonable number of consumer reports or investigative consumer reports, or to average an unreasonable number of said completed reports per day or other period;

(2) quotas for adverse information, as defined herein, which require or compel its investigative personnel to complete or prepare a certain proportion of consumer reports or investigative consumer reports, containing negative or derogatory information about the consumers who are the subject of the reports; and

(3) paying or "crediting" an investigator for a reinvestigation conducted pursuant to Section 611 of the Fair Credit Reporting Act only if the reinvestigation proves that the investigator was accurate in his initial investigation.

PAR. 21. By and through the use of these aforesaid procedures, and others similar thereto, but not expressly set out herein, respondent imposes requirements and pressures upon its investigative personnel which are inconsistent with accurate reporting and which have the tendency and capacity to promote incomplete or inaccurate reports. Therefore, respondent has failed and is failing to adopt reasonable procedures to assure the maximum possible accuracy of the information concerning the individuals about whom the reports relate, as required by Section 607(b) of the Fair Credit Reporting Act.

PAR. 22. In the ordinary course and conduct of its business, as

aforesaid, respondent has been and is being requested by consumers, who properly identify themselves, to disclose information in its files on the consumers. In response to these requests, in certain instances, respondent fails to clearly and accurately disclose the nature and substance of all information (except medical information) in its files at the time of the request. Further, unless specifically requested by the consumer in each instance, respondent fails to disclose:

(1) the sources of the information (except investigative sources, which need not be disclosed); and

(2) the recipients of any consumer report on the consumer which it has furnished for employment purposes, within the two-year period preceding the request, and for any other purpose within the six-month period preceding the request.

PAR. 23. By and through the use of the practices described in Paragraph Twenty-Two above, respondent has violated and is violating the provisions of Section 609 of the Fair Credit Reporting Act.

PAR. 24. In the ordinary course and conduct of its business, as aforesaid, respondent, in certain instances, has failed to disclose the information in consumers' files pursuant to Section 609 of the Fair Credit Reporting Act when requested to do so by telephone, or has discouraged such disclosures. Further, respondent has refused and is refusing to make said disclosures at offices designated by respondent as "Sub-Offices", even when some of those offices are staffed by full-time office personnel and a person in a supervisory capacity. Rather, respondent makes disclosures only at offices designated by it as "Branch Offices".

PAR. 25. By and through the use of the practices described in Paragraph Twenty-Four above, respondent has violated and is violating the provisions of Section 610 of the Fair Credit Reporting Act.

PAR. 26. In the ordinary course and conduct of its business as aforesaid, respondent, in certain instances:

(1) fails to reinvestigate items of information, the completeness or accuracy of which is disputed by the consumer;

(2) fails to record the current status of disputed information and to promptly delete information which can no longer be verified;

(3) fails to clearly and conspicuously disclose to the consumer his right to request that respondent furnish notification that a previously reported item of information has been deleted or that respondent furnish a statement prepared by the consumer (or a clear and

accurate codification or summary thereof) to recipients of previous reports; and

(4) fails to provide said notifications to recipients of previous reports (within the past two years for employment purposes and the past six months for any other purpose) when specifically requested to do so by the consumer.

PAR. 27. By and through the use of the practices described in Paragraph Twenty-Six above, respondent has violated and is violating the provisions of Section 611 of the Fair Credit Reporting Act.

PAR. 28. In the ordinary course and conduct of its business as aforesaid, respondent retains file copies of the information contained in the consumer reports and claims reports which it prepares for its customers. Respondent incorporates all of said information into the same filing system, making no attempt to segregate the consumer report information from the claims report information. In the preparation of subsequent consumer reports and claims reports, respondent uses all of its file information interchangeably, including the use of claims report information in the preparation of consumer reports and the use of consumer report information in the preparation of claims reports.

However, with respect to said claims reports, respondent fails to observe the provisions of the Fair Credit Reporting Act which regulate the preparation and dissemination of information which is used or expected to be used in consumer reports.

PAR. 29. By and through the use of the practices described in Paragraph Twenty-Eight above, respondent has failed and is failing to comply with Sections 605, 607(b) and 614 of the Fair Credit Reporting Act with respect to the preparation of consumer reports, and Sections 604 and 607(a) of that Act with respect to the dissemination of consumer reports.

PAR. 30. The acts and practices set forth in Paragraphs Fifteen through Twenty-Nine, above, were and are in violation of the Fair Credit Reporting Act, and pursuant to Section 621(a) of that Act, said acts and practices constitute unfair or deceptive acts or practices in commerce in violation of Section 5(a) of the Federal Trade Commission Act.

Initial Decision by Theodor P. von Brand, Administrative Law Judge

November 11, 1977

Preliminary Statement

This is a case under Section 5 of the Federal Trade Commission Act (FTCA) and the Fair Credit Reporting Act (FCRA). The Commission complaint, dated February 21, 1974, charges Equifax Inc., a consumer reporting agency, with violation of these statutes in connection with the preparation, dissemination and sale of consumer reports[1] and consumer investigative reports.[2] Respondent's answer denied the material allegations of the complaint.

Count I of the complaint, which contains the charges of Section 5, FTCA violations, involves allegations of deceptive and unfair acts. The charges are essentially the following: [3]

1. Respondent's investigative personnel, it is alleged, have misrepresented in certain instances, to consumers that they are the agents or employees of the companies to which the consumers have applied for benefits such as an insurance company and/or that the information furnished by the consumers or others during interviews will be used exclusively by the companies to which the consumers have applied for benefits. It is further alleged that some of those interviewed would have elected to provide the information directly to the companies from which benefits were sought rather than to respondent had they known the true identities of the interviewers or that such data would be added to respondent's files for future reference (Complaint, Pars. 5, 6).

2. It is alleged that respondent's investigative personnel have misrepresented the purposes of investigations by representations such as that a credit check was being conducted when, in fact, in certain instances, the purpose of the investigation was to evaluate a consumer claim for loss or injury under an insurance policy and the object of the interview was to observe the consumer's appearance

[1] "(d) The term 'consumer report' means any written, oral, or other communication of any information by a consumer reporting agency bearing on a consumer's credit worthiness, credit standing, credit capacity, character, general reputation, personal characteristics, or mode of living which is used or expected to be used or collected in whole or in part for the purpose of serving as a factor in establishing the consumer's eligibility for (1) credit or insurance to be used primarily for personal, family, or household purposes, or (2) employment purposes . . . ." (Section 603(d) FCRA).

[2] "(e) The term 'investigative consumer report' means a consumer report or portion thereof in which information on a consumer's character, general reputation, personal characteristics, or mode of living is obtained through personal interviews with neighbors, friends, or associates of the consumer reported on or with others with whom he is acquainted or who may have knowledge concerning any such items of information . . . ." (Section 603(e) FCRA).

and the consumer's mental or physical capacity in connection with such investigation (Complaint, Pars. 7, 8).

3. Respondent, it is alleged, has represented that interviews are conducted in person rather than on the telephone, that direct observation of the consumer's environment is conducted and that all sources of information listed are seen. The complaint charges that, in certain instances, interviews were conducted on the telephone rather than in person, that the consumer's environment was not directly observed, and the sources listed on the consumer report were not interviewed in person or on the telephone. The complaint alleges that users of such reports would not have given as much weight to the information provided by respondent had the manner in which such reports were prepared been truthfully and factually represented (Complaint, Pars. 9, 10). [4]

4. It is alleged that respondent, through the use of authorizations, for the release of medical information, obtained from insurance companies,[3] represents directly or by implication to medical personnel from which such information is sought that the data is secured for the exclusive use of such insurance companies. The complaint charges that consumers executed such authorizations on the basis of that belief. It is further alleged that, in truth and in fact, the information is not obtained for the exclusive use of the insurance company to which the authorization was executed but is retained by respondent and, in certain instances, is utilized in the preparation of subsequent reports for different customers of respondent. Some consumers, it is alleged, would not authorize the release of such confidential information if they knew it would be utilized by a third party such as a consumer reporting agency (Complaint, Pars. 11, 12, 13).

The Count II charges focusing specifically on the FCRA may be summarized as follows:

1. Respondent, it is alleged, furnishes information to persons which it has no reason to believe intend to use such data for one of the permissible purposes set out in Section 604, FCRA (Complaint, Pars. 16, 17).

2. Respondent, it is alleged, reports the existence of adverse obsolete information in violation of Section 605, FCRA (Complaint, Pars. 18, 19). [5]

3. Respondent's requirements and pressures on its investigative

[3] According to the complaint, the authorizations obtained by respondent from insurance companies are photocopies of originals signed by the consumers but are silent as to the release of such information to anyone other than the insurance companies, including the respondent.

personnel are inconsistent with accurate reporting and have the tendency and capacity to promote incomplete or inaccurate reporting. As a result, respondent, it is alleged, has failed to adopt reasonable procedures to assure maximum possible accuracy in its reports as required by Section 607(b), FCRA (Complaint, Pars. 20, 21).

4. Respondent, it is alleged, has violated the disclosure provisions of Section 609, FCRA, in certain instances, by failure to clearly and accurately disclose the nature and substance of all information (except medical information) in its files at the time of request. It is further alleged that, unless specifically requested by the consumer in each instance, respondent fails to disclose requested information such as (a) the sources of information (except investigative sources which need not be disclosed); (b) the recipients of any consumer report on the consumer which it has furnished for employment purposes within the 2-year period preceding the request, and for any other purpose within the 6-month period preceding the request (Complaint, Pars. 22, 23).

5. It is alleged that respondent fails to disclose information in the consumer's file pursuant to Section 609 of FCRA when requested to do so by telephone or discourages such disclosures. It is further alleged that respondent refuses to make such disclosures at its "sub offices" even when some of these offices are staffed by full-time personnel and a person in a supervisory capacity. It is further alleged that respondent makes disclosures only at those offices which it has designated as branch offices. These practices, it is alleged, violate Section 610, FCRA (Complaint, Pars. 24, 25). [6]

6. Respondent, it is alleged, has violated Section 611, FCRA, by failing to reinvestigate disputed information; failing to record the current status of disputed information and to promptly delete information which can no longer be verified; failing to clearly and conspicuously disclose to the consumer his right to request that respondent furnish notification that a previously reported item has been deleted or that respondent furnish a statement prepared by the consumer to recipients of previous reports; and finally, by failing to provide notification to recipients of previous reports (within the past 2 years for employment and the past 6 months for any other purpose) when specifically requested to do so by the consumer (Complaint, Pars. 26, 27).

7. It is alleged that respondent's filing system incorporates claim reports and consumer reports in the same file with no attempt to segregate the consumer report information from the claim report information. The complaint charges that in the preparation of

subsequent consumer reports and claim reports that respondent uses all of the file information interchangeably, using claim report information in the preparation of consumer reports and consumer report information in the preparation of claim reports. The complaint alleges that such practices violate the FCRA provisions regulating the preparation and dissemination of consumer reports in Sections 605, 607B, 614, 604 and 607, FCRA (Complaint Pars. 28, 29).

After extensive evidentiary hearings, the record was closed on June 15, 1977. [7]

This matter is now before the undersigned for decision based on the allegations of the complaint, the answer, the evidence and the proposed findings of fact, conclusions, and briefs filed by the parties. All proposed findings of fact, conclusions and arguments not specifically found or accepted herein are rejected. The undersigned, having considered the entire record and the contentions of the parties, makes the following findings of fact and conclusions, and issues the order set out herein.

Findings of Fact

I. Respondent and the Nature of Its Business

1. Equifax Inc. (formerly Retail Credit Company, a corporation) is a corporation, organized, existing and doing business under and by virtue of the laws of the State of Georgia, with its principal place of business located at 1600 Peachtree St., NW., Atlanta, Georgia (CX 1445A; Burge 5070).

2. Effective January 1, 1976, the name Retail Credit Company was changed to Equifax Inc. (Burge 4847, 4852).

3. Equifax Inc. is the parent corporation of some 14 companies and divisions, some of which are separately incorporated; some are autonomous operating divisions. While these companies perform in special markets, they are all in the information industry furnishing personal information to parties requiring data on which to base business decisions, primarily in connection with insurance, employment, and credit transactions (Burge 4848; CX 666Z–12). [8]

4. Equifax Services, which was the largest of respondent's autonomous units, was a division of Equifax Inc. Its operations are the subject of this proceeding. This division was originally the insurance reporting and commercial reporting arm of Retail Credit Company (Burge 4848).

5. Equifax Services furnished consumer and consumer investigative reports to insurance companies for underwriting purposes,

including life, health, fire, property and automobile insurance. It conducted claim investigations, furnished financial reports, and prepared employment reports, as well as credit reports, in isolated areas where there are few credit bureaus (Burge 4850–51). Reporting on insurance applicants comprised the bulk of its business (CX 679E). Insurance customers were considered its "basic field" (RX 107D).

6. Prior to January 1, 1976, Retail Credit Company had general supervision of the business which became Equifax Services (Burge 4853).

7. On April 1, 1977, Equifax Inc. created a wholly owned subsidiary corporation, Equifax Services, Inc., which provides the reporting services performed before that date by the Equifax Services division (RX 916).

8. Other affiliated companies[4] are: Equifax Services, Limited, which performs in Canada the same activities as does Equifax Services, Inc. in the United States (Burge 4848); Atwell, Vogel and Sterling, Inc., a company providing reports for audit-inspection and loss control services for property, casualty and inland marine underwriters (RX 107G); Hunnicutt & Associates, Inc., which is in the business of property appraisal and mapping (RX 107G); Physical Measurements, Inc., which furnishes medical examinations in connection with insurance applications (RX 107G); the Credit Bureau [9]Companies, which perform the functions which their name implies (RX 107G–H); Retailers Commercial Agency, whose primary work is making credit reports on the telephone, principally in connection with mortgage loans, and which handles most of respondent's telephone reporting (Knautz 6881–82); Gay and Taylor, which is engaged in claims adjusting services (Trotochaud 6288); Credit Marketing Services, a separate corporation providing credit reporting services to credit grantors; Retrieval Services, a division of respondent providing the service of picking up credit cards from delinquent consumers; Marketing Services, a division of Equifax Inc., doing market research; and International Printing and Distributing, a division of respondent engaged in printing for respondent and commercial printing for outside customers (Burge 4848–49).

9. Respondent, in the ordinary course and conduct of its business and subsequent to April 25, 1971, has been engaged in the preparation, offering for sale, sale and distribution of information on consumers, including consumer reports and investigative consumer reports (CX 1445C).

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[4] No evidence was introduced with respect to the operations of these companies.

10. In the ordinary course and conduct of its business, respondent causes and for some time in the past has caused reports including claims reports, and subsequent to April 25, 1971, consumer reports and investigative consumer reports, to be distributed through the mail from its branch offices and other offices located throughout the United States to its customers located in various other States of the United States (CX 1445C).

11. Respondent maintains, and at all times mentioned in the complaint has maintained, a substantial course of trade in the aforesaid services, including consumer reports, investigative consumer reports, and claims reports, in commerce, as "commerce" is defined in the Federal Trade Commission Act (CX 1445C). [10]

12. In 1972, respondent's total revenues were $195,262,000, and its income before taxes was $17,460,000. These figures include all of respondent's operations (including Canada) and all of its subsidiaries (CX 1445C). Respondent's total claim volume was $26,749,557 in 1975 (Trotochaud 6291).

13. Respondent sells information about consumers to business customers numbering in the thousands. As of July 15, 1974, it had approximately 17,000 customers[5] (CX 1445B).

14. In 1971, respondent issued approximately 22.5 million reports of all types to customers in the United States.[6] For 1973, the corresponding figure was 21 million.[7] (CX 1445B).

15. During the period from March 1971 to May 1974, respondent maintained files containing information concerning approximately 45 million persons[8] (CX 1445B).

II. THE REPORTS AND SERVICES FURNISHED BY RESPONDENT

16. The reports prepared by respondent may generally be categorized as follows: underwriting reports to facilitate underwriting by insurance companies, employment or personnel selection reports, financial control reports and claim reports (see generally Stansbury 6735 [11]et seq.; Hopp 6683 et seq.; Knautz 6870 et seq.; Trotochaud 6724 et seq.).[9]

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[5] These figures pertain to respondent's operations in the United States, and do not include figures obtained from respondent's subsidiaries (CX 1445B).

[6] This does not include figures obtained from respondent's subsidiaries (CX 1445B).

[7] This figure pertains to respondent's operations in the United States, and does not include figures obtained from respondent's subsidiaries (CX 1445B).

[8] This figure pertains to respondent's operations in the United States, and does not include figures obtained from respondent's subsidiaries (CX 1445B).

[9] This section is not intended to catalogue exhaustively all of respondent's reports. It is intended to be illustrative and to generally outline the range of services available and the more significant reports which respondent offers.

A. The Underwriting Reports

17. Respondent's underwriting reports fall into two major groups: Life and Health reports and Fire and Casualty reports (see RX 316A-D, 315A-D). For such reports, respondent charges basically two rates: a "L & H charge for standard or regular reports in any given locality" (RX 315A) and a "fire and casualty rate charge for standard or regular reports in any given locality" (RX 316A). In addition, an hourly fee "per hour for time required on special or expanded investigations" may be charged (RX 315A, 316A).

18. In 1973, the L & H charge was $5.35 and the fire and casualty charge was $5.60 (RX 566 III-7, 315, 316).[10] Reports charged at the basic rate, *e.g.*, $5.35, are also referred to in the record as "single fee" reports.

19. Respondent considers two of its underwriting reports, the Regular Life report and the Regular Auto report, which are the most frequently handled reports, as its two basic services (RX 566 III-6).

(1) Life Reports

20. CX 422A is the Form 1 basic life report used until the end of 1975. It was used to aid respondent's customers in the underwriting of small life insurance applications (Stansbury 6746). The basic rate was charged for this report, and there was a requirement that two sources be contacted as part of its preparation. [12]

21. The applicant or an adult member of his household counted as a source. If the applicant were contacted and interviewed, then a minimum of one additional source had to be interviewed[11] (Stansbury 6747). The basic life report could be handled at either the applicant's business or neighborhood location or at both (Stansbury 6748).[12] Time coverage[13] in the case of this report was 2 years, meaning that the sources interviewed had to have been acquainted with the applicant for 2 years (Stansbury 6745, 6748).[14]

22. The basic life report was to be completed by in-person handling by the field representative, but if this proved impossible, the telephone could be used (Stansbury 6750).

23. The Streamlined Life report was a report whose rate was 25

[10] In certain locations, the L & H and F & C charge may have been higher or lower (RX 315B, 316B).

[11] An employment source would then be sufficient to complete the report.

[12] The term "location" in this context means the general area where the interviews were to be handled. In the case of some reports, the interviews may have been required at more than one location, *i.e.*, a business and neighborhood location (Stansbury 6748).

[13] Time coverage is the total time sources need to have known the subject of the report required in the case of a particular report service offered by respondent (Stansbury 6745).

[14] Such coverage for a 2-year period could have been achieved even though each source knew the applicant for only one year provided that together they covered the 2-year time span (Stansbury 6745).

cents less than basic. It was designed to meet the desire for a full scope investigation with limited feedback at a lesser price. Remarks were not covered in narrative form, and the answers were given by checking various blocks. The report could be handwritten, and the heading on the report was prepared by the customer (Stansbury 6765–66). [13]

24. The NORS Service or Notification or Report Service was a service where a notification, but no report, was filed when there were no unfavorable facts found and the insurance application was relatively small. This service was used in connection with basic rate reports or reports less than basic rate (Stansbury 6775–76).

25. The RAPCON Service, like NORS, was designed to speed up handling and to limit clerical functions. It was transmitted by telecommunications if the report was completely favorable to the subject. In the event that the case was not favorable, a report was filed (Stansbury 6776).

26. The NORS Service was generally priced at less than the basic rate while RAPCON was a few cents over the basic charge (Stansbury 6777).[15]

27. Other life reports calling for more information or greater detail were priced at multiples of the basic rate; such reports are referred to in the record as multiple fee reports. For example, CX 487, the "Intermediate Life or Health Report" was priced at double the basic rate; its time coverage was 3 years, and the minimum number of sources to be seen was three. On this report, two locations were required; namely, a business and a residential location. The purpose of this report was to give more information than the basic life report on applications for insurance policies with larger limits (Stansbury 6770–71).

28. The Special Narrative Life report, CX 412, one more step up the ladder, had time coverage of 5 years, the minimum sources to be contacted were four, and the required locations were business and residential. It was priced at three times the basic rate. The telephone [14]could be used only after personal efforts had been made to complete the handling (Stansbury 6771–73). This report had greater detail than the Intermediate report because of the narrative treatment (id.).

29. CX 420, the Special Life Specific Rate report, was priced at six times the basic rate. The required number of sources was six. Time

[15] The NORS Service was less than basic because no report had to be filed. In the case of RAPCON, the NORS rate applied, but there was a surcharge for the RAPCON telecommunications service. Generally, NORS was 25 or 35 cents less than the basic charge (Stansbury 6777).

coverage was 7 years, and the locations to be covered were two or more (Stansbury 6779).

30. CX 432, the Special Life report, was an hourly rate report. The time coverage was a quarter of the applicant's lifetime, and as many sources and locations as needed to develop the information were required. This report was the "Cadillac" or the top of the line of the Life Series. It was a service designed to get complete information in the case of larger insurance applications with particular emphasis placed on finances (Stansbury 6781).

31. Subjective features, such as the habits of the person being reported on, were covered equally on all the reports (Stansbury 6780).[16]

(2) Health Reports

32. CX 413 was the basic health report. It was priced at the basic rate, had time coverage of 1 year and required a minimum of two sources. It was comparable in scope to the basic life report but put emphasis on factors bearing on morbidity, viz., frequency of disability, rather than mortality. It was used in connection with disability or loss of time insurance (Stansbury 6785–87). There was greater emphasis on finances in this health report than in the basic life report in order to throw light on the motivation to work following a disability (Hopp 6786–87). [15]

33. CX 427 was the Special Narrative Health report. It was priced at triple the basic rate, had time coverage of 5 years and required a minimum of four sources (Hopp 6795). The depth of the report was greater because of the additional time coverage and because more emphasis was placed on finances than in the case of single fee reports (Hopp 6796).

(3) Casualty and Property Reports

34. Respondent serves the entire property and casualty insurance industry embracing some 27 different types of insurance policies ranging from automobile through property insurance (Hopp 6684).

a. Automobile Reports

35. Respondent's automobile reports fall into two general categories and, within each, there are a variety of different reports whose use depends upon the coverage desired by a particular insurance

[16] Subjective information is information obtained through outside sources and pertains to an individual's personal activities (Stansbury 6780–81).

company. In the first group, respondent offers full automobile services which consist of reports of an investigative consumer nature, including general information on the applicant. The second category comprises the classification type service, focusing primarily on the uses and drivers of vehicles in a household, *e.g.,* number of cars and their principal operators (Hopp 6685).

36. There are several basic full auto reports. The principal of these reports is Form 6033, CX 479, which is the most frequently used full auto report form (Hopp 6685, 6698).

37. In a full auto report, the general requirements are a year's time coverage and generally an interview with the applicant and one outside source. In the event that the applicant cannot be interviewed, then a minimum of two outside sources is required (Hopp 6686).

38. Respondent has approximately 16 to 18 report forms for its full or basic auto reports (Hopp 6687). Most of the full reports are at the flat rate or property and casualty rate. There are also some reports at multiples of that rate (Hopp 6688). [16]

39. Certain of the full automobile reports may be filled out in longhand, and these are referred to as streamlined reports (Hopp 6689).

40. The classification reports facilitate the insurance company's classification and rating system; namely, the determination of in which classification category a particular risk falls. This decision is based on such information as age group, marital status, usage of car, approximate mileage and where the car is kept (Hopp 6690).

41. In terms of the number of auto reports completed in 1972, classification type reports represented approximately 5 percent of respondent's total volume (Hopp 6691).

42. There is a wide variety of classification report forms because classification categories differ by insurance companies and in different parts of the country. For example, the institution of "no fault" insurance in certain states necessitates separate forms for those states. Respondent uses approximately 50 different report forms in connection with the classification and rating services (Hopp 6691). Some auto classification reports are telephone reports, whereas others are to be handled on the street (Case 6023–24).

43. In the case of the classification service, requirements as to interviews with the applicant, time coverage and other factors vary widely depending upon the desires of the particular customer of respondent (Hopp 6691–92).

44. The classification reports are completed in longhand since they primarily consist of "yes" or "no" answers with few or no

narrative remarks. Generally, they are less expensive than the full auto reports (Hopp 6692). There is a wide variety of prices available in this category of reports based upon the effort required (Hopp 6693). [17]

b. Property Line Services

45. In the property line services, respondent offers five basic services (Hopp 6708–09), but 100 or more reports are available in this line (Hopp 6716).

46. The first group is comprised of the Modified Short Form report, which requires only observation of the property to be insured and a photograph, if requested.[17] No interview is required, and such reports are completed in longhand (Hopp 6708–09). These reports are charged at less than the basic rate because the effort factor is not considered as great as in the standard report (Hopp 6709).

47. The second category is respondent's Dwelling, Fire Short Form report, which is also an observation service. This report, over and above the Modified Short Form information, includes an estimated replacement cost figure and certain construction features. Outside sources are not involved in the preparation of this report, but an interview with the applicant is to be attempted. This report also is priced at less than the basic fee (Hopp 6709–10).

48. The third category is the Dwelling Fire report, which is respondent's standard service and is considered a full scope report requiring a year's coverage, contact with the insured and outside sources, or with outside sources only, if the insured cannot be interviewed. It is rated at the property and casualty rate and is typed (Hopp 6710). [18]

49. The fourth category is the Streamlined Homeowner's report, the cost of which is somewhat greater than the fire report. This report, in addition to information relevant to fire coverage, includes information on theft and liability exposure (Hopp 6711). The Streamlined Homeowner's report requires an interview with the applicant and an outside source, or one outside source if the applicant can't be interviewed. One-year coverage is required, and it is done in longhand (Hopp 6711).

50. The fifth report is a Full Homeowner's report. The scope of the information covered is basically the same as in a Streamlined report, but the report is typed. It is more expensive than a Streamlined report (Hopp 6711).

[17] In the case of all property reports, a photograph is available, but there is an extra charge for that service (Hopp 6712).

B. Employment or Personnel Selection Reports

51. Prior to January 1, 1976,[18] respondent offered three basic employment reports to the insurance industry. The Agent L & H report, the Special Narrative Agent report and the Special Agent report (Knautz 6873).

52. The Agent L & H report had a year's time coverage, and the minimum sources were the subject of the report and file information or two outside sources. The report was priced at the personnel rate[19] (Knautz 6873–74).

53. The Special Narrative Agent report had time coverage of 5 years, and the minimum number of sources to be contacted was three. It was priced at three basic L & H rates (Knautz 6874). **[19]**

54. The Special Agent report, priced at an hourly rate, had time coverage of a quarter of a subject's lifetime, and as many sources as necessary were to be seen. The customer had the option of setting a limit on the amount of time spent by the field representative (Knautz 6875).

55. Reports in the personnel selection area not confined to the insurance industry, afforded a similar spectrum for depth of coverage. Prices for these reports ranged from a single fee "personnel rate"[20] when the investigation was conducted at one location, to multiple fee and hourly rates[21] and flat rate reports[22] (RX 328A; Knautz 6878–81). **[20]**

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[18] Subsequent to this date, respondent restructured the agency services (Tr. 6875).

[19] See page 18, for definition of "personnel rate."

[20] The "personnel rate" as of January 1, 1972, was $4.85; the "security personnel selection rate" was $5.25; and the hourly rate was $10.20 (RX 328B).

[21] The number of fees or personnel rates to be charged for certain reports depended on the number of locations visited by the field representative. *E.g.,*

Service	*Charge Basis*
PERSONNEL SELECTION REPORTS	
A. One location	Personnel Rate
B. Two or three locations	Double Personnel Rate
C. Four or more locations	Triple Personnel Rate
D. Correspondent territory	Maximum Charge Double Personnel Rate

(Price List—June 1, 1972, RX 328A.)

[22] If a customer chose a "flat rate report," he received a full 5-year report regardless of the number of locations visited. The field representative would be compensated for normal amount of time spent and on a per-location basis. If the field representative went to more than one location, he would be compensated on the number of locations visited (Knautz 6879–80). Respondent had the following flat rate personnel selection services available as of June 1, 1972:

PERSONNEL SELECTION REPORT (Report covers most recent 5 years)	$21.45
SECURITY PERSONNEL SELECTION REPORT (Report covers most recent 5 years)	$24.50
SPECIAL PERSONNEL SELECTION REPORT	

(Continued)

C. Financial Control Services

56. Respondent's financial control services include audit and validation services, credit reports, and collection aid services (Knautz 6892).

57. The audit and validation service is essentially a physical audit of inventory for institutions such as banks, which engage in inventory financing (Tr. 6893).

58. Respondent also offers business credit reports, character financial reports and individual credit reports (Knautz 6893).

59. Respondent's collection aid services include current asset and income reports, slow payer reports, credit card pickups and location reports (Knautz 6895).

D. Respondent's Claim Service

60. Respondent's claim service generally includes investigations relating to death, health, disability, sickness, accident and continuing disability claims (Trotochaud 6291). Respondent's claim service is sold to two segments of the insurance industry: the life and health companies and those firms engaged in the fire and casualty field (Trotochaud 6291–92).

61. In the life and health fields, respondent does primarily reports on first-party claimants, viz., a claimant insured by the company with whom he has filed a claim. Third party claim investigations involving individuals filing claims against companies other than the ones with which they are insured, are generally conducted for casualty insurance companies such as auto insurers (Trotochaud 6298). [21]

62. Respondent charges for its claim reports on a flat rate and an hourly basis. Approximately 65 percent of respondent's claim revenues are derived from hourly rate investigations where a charge is made for the time spent. The remaining claim investigations are charged at a flat rate which may be a single claim rate or multiples thereof[23] (Trotochaud 6300–01).

63. The Late Progress report is an example of a single flat fee report. It is designed to give the insurance company information as to whether a total disability claimant is still disabled and still alive.

(Report covers most recent 1/4 lifetime) $47.00
SALESMEN SELECTION REPORT
(Report covers most recent 1/4 lifetime) $49.00
EXECUTIVE QUALIFICATION REPORT
(An exhaustive tailor-made investigation, specially presented) $350.00
(RX 328A.)

[23] In 1972, the single claim rate was $4.85, and the hourly rate charge was $10.20 (RX 337B).

On this type of investigation, two outside sources are to be contacted (Trotochaud 6301).

64. A Continuance of Disability report is an example of a double claim rate report. On that report, respondent attempts to determine whether a claimant, accepted as disabled, is still disabled. In the case of this report, at least two outside sources and the claimant are to be seen (Tr. 6301–02).

65. The Personal Injury report is an example of a report for which four single claim rates are charged. It is used in the case of third-party claimants; outside sources and the claimant are to be interviewed. The service also includes a record check for such items as past accidents (Trotochaud 6302–03).

66. Hourly rate claim reports are termed "special investigations." Typically, in the case of a death claim investigation, there is a limit of $95.00. The field representative may expend time up to the limit, and the customer is contacted for authorization to continue in the event the investigation is not completed (Tr. 6303). There is no minimum number of sources to be contacted in the case of an hourly rate claim report (Tr. 6304). [22]

67. Field representatives have, as a practical matter, set a time limit on flat rate claim reports. The charge for a double claim rate report is approximately the same as the hourly charge. In the case of a double fee report, the field representative generally works the case for an hour, and if more remains to be done, the customer is requested to advise whether additional work is desired (Trotochaud 6306–07).

68. The Underwriting Medical History report is a service within the jurisdiction of the Claims Department, although it is not a claim report. In it, respondent secures medical information from sources such as physicians and hospitals, in order to expedite the flow of medical information to insurance companies (Trotochaud 6282).

III. RESPONDENT'S ORGANIZATION AND STRUCTURE

69. Respondent operates essentially at three levels: its Home Office; the operating regions; branch offices, suboffices and detached local units (DLUs) (CX 666D).

70. The Home Office, located in Atlanta, Georgia, formulates policy for the company, controls its operations and performs service functions such as accounting, sales, research, education and other staff work, which can be best done from a central point (CX 666D).

71. There are 15 regions in the United States, which have

administrative and supervisory responsibility over the branch offices located in their territory (Jones 5125).

72. Branch office managers report to a Regional Vice President, who generally is responsible for 13 to 15 branch offices (Jenkins 5644).

73. A Regional Vice President, in turn, reports to a vice president and associate operating manager in respondent's Home Office in Atlanta (Jenkins 5645). [23]

74. A Regional Vice President, who supervises the branch office managers directly, is the extension of respondent's home office management, responsible for meeting quality and financial objectives in the region. In this connection, he is also responsible for the movement of business, meeting time service, employee morale and maintenance of facilities individually for the branch offices and collectively for the region. Other responsibilities include staffing the offices and manpower development for the corporation (Lieber 8978–79).

75. Preparation of the consumer and consumer investigative reports under consideration here is carried on by respondent's branch offices in the field and their related suboffices (numbering respectively some 219 and 1,000 in April 1976) (Jones 5125).[24]

76. The personnel in branch offices varies with the size and type of office. A branch office always has a manager and sometimes one or more assistant managers.[25] It also has a number of firstline supervisors responsible for supervising, on a daily basis, the work of one to six field representatives. Such supervisors spend part of their time supervising and the balance of their time preparing reports (Jenkins 5697–98). A branch office may also contain a claim director and a supervisor of the unit making employment reports—a personnel selection director. Included in supervisory personnel is the branch office trainer who trains new field representatives (Jenkins 5698). [24]

77. Branch offices also employ service reviewers who have the responsibility of reviewing written reports after they are dictated by the field representative and typed by the stenographer. The reviewer is generally the most experienced and highly trained clerical person in the office. If she finds a discrepancy in a report, such as an

[24] Respondent had 272 branch offices as of February 25, 1972, while the corresponding figure for May 10, 1974 was 229. In both years, at least one such office was located in each state with the exception of Vermont and the District of Columbia (CX 1445A). In addition, as of March 31, 1972, respondent had approximately 1,055 suboffices, the corresponding figure for December 31, 1973, being 994 (CX 1445B). These figures pertain to respondent's United States' operations and do not include figures from its subsidiaries (CX 1445A–B).

[25] Branch managers, in addition to their other duties, also have a responsibility to obtain and keep local business from agents in their area (Shaffer 8396).

incomplete report, it is her responsibility to get the report back to the supervisor of the field representative involved (Jenkins 5699).

78. Most branch offices contain "regular" units which include the field representatives designated to handle basic rate reports, which are distinguished from claim investigations, special life reports or personnel reports. The regular units contain a cross section of respondent's employees. New employees enter these units, as a general rule, but they may also contain those field representatives with greater experience who have not shown an aptitude for handling claim investigations or the more sophisticated reports (Jenkins 5711–12).[26]

79. In addition to the regular units, branch offices may have specialized units such as special life units, personnel units, property line units and claim units (Curtis 7093, 7115). Once expertise and length of service are developed, field representatives are usually given more specialized investigations (Deibig 13752).

80. A suboffice is an office within a branch office's territory located at a distance from the branch office.[27] Suboffices do not maintain full file storage systems and do not have full responsibility over their territories other than in producing reports (Jones 5125). Detached local units function like suboffices but are in closer geographic proximity to the branch office (id., Jenkins 5828). [25]

81. It is respondent's policy that field representatives in suboffices should be "better than average" because they work without direct supervision. Their work requires the ability to operate successfully away from close contact with management (RX 107Z–140). The detached local unit, while it operates like a suboffice, receives close supervision from the branch office management because of its proximity to that office (RX 107Z–142).

82. Respondent's claim services are under the jurisdiction of the Claim Department in the Home Office, which has been in existence since 1973 (Trotochaud 6331).[28]

83. In the field, respondent has 17 Regional Staff Managers, Claims, approximately 200 claim directors in the branch offices and 600 to 650 full-time claim field representatives (Trotochaud 6276–77).

84. The regional claim supervisor or staff manager shares responsibility with the branch manager for superintending and

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[26] In the case of the more sophisticated special life reports, for example, it is necessary for the field representatives to be able to read financial statements and be acquainted with concepts such as unearned income (Jenkins 5713).

[27] Suboffices are divided into two categories. The Class A suboffices are the larger suboffices while the Class B suboffices are smaller and in more remote and less populous areas (Matthews 5568).

[28] Prior thereto, the claim operations were conducted by a division of the Operating Service Department (Trotochaud 6331).

developing claim personnel. In addition, he has sales responsibility for the claim service in his region (Jones 5135–36).

85. The branch office claim director, who reports directly to his branch manager, has complete responsibility for the claim service in his office. He directly supervises the claim field representatives in the branch and suboffice territory (Trotochaud 6279). In a small branch office, the claim unit may consist of the claim director alone (Trotochaud 6284).

86. Claim work is considered a specialty program in the branch office. It particularly lends itself to specialization in terms of placing field representatives into specialized units for developing job skills in that particular area (Jones 5136–37). A full-time claim investigator is a field representative who devotes 80 percent or more of his time to claim work (Trotochaud 6285). [26]

87. Field representatives engaged in claim work need more expertise and talent than those field representatives working in a regular unit such as the life and auto unit (Monarch 8570, 8574).

IV. RESPONDENT'S FIELD REPRESENTATIVES

A. General Characteristics

88. Respondent's field representatives perform the investigative work underlying the reports with which this proceeding is concerned. Field representatives are either full-time, salaried employees or part-time employees paid on a per unit basis.

89. As of May 10, 1974, respondent had approximately 4,635 salaried field representatives out of its total of 7,413 salaried employees (CX 1445B).[29] During 1971, it had an average of 4,486 non-salaried employees (excluding subsidiary employees); of this total, 1,775 employees were regular part-time field representatives (CX 1445B).[30]

90. A new salaried field representative must be 21 years of age and a high school graduate, although respondent prefers that he or she has more education (Jenkins 5715). A background check is conducted on every employee (Tr. 5717).

91. Respondent's field representatives, in terms of educational achievement, may be grouped as follows for the period 1971–1975: [27]

[29] As of January 27, 1971, out of a total of 9,249 employees, respondent had 5,910 salaried field representatives (excluding U.S. subsidiaries).

[30] The function of the regular part-time field representatives is primarily to handle volume in peak periods (RX 107Z–80).

Educational Levels of Retail Credit Company Field Representatives On Hand at End of Each Year (United States and Canada)

Calendar Years 1971—1975

Educational Level	*1975*	*1974*	*1973*	*1972*	*1971*
High School Graduate	36%	39%	39%	42%	42%
College Undergraduate	39%	36%	37%	37%	39%
College Graduate	25%	25%	24%	21%	19%

Educational Level of New Retail Credit Company Field Representatives Hired Each Year (United States only)

Calendar Years 1971—1975

Educational Level	*1975*	*1974*	*1973*	*1972*	*1971*
High School Graduate	17%	15%	15%	27%	17%
College Undergraduate	40%	44%	43%	37%	45%
College Graduate	43%	41%	42%	36%	38%

(RX 728.)

92. Respondent's Branch Manager's Manual, dated December 1968, indicates that education plays the following role as a consideration in hiring:

Particularly in view of the Company's practice of promoting from within, it is desirable that a good proportion of Inspectors have some college training. However, high school graduation is acceptable, *providing the applicant had a credible scholastic record.* In hiring men with college training, it is generally desirable that this training shall have been acquired at a small college, since men from such schools would be inclined to be more satisfied with average earnings and difficult working conditions than would men from the larger, more socially prominent institutions.

(CX 673Z–10.) [28]

93. Respondent views single applicants for employment favorably for the following reasons:

In view of the moderate starting salary paid to Inspectors, many married men with family responsibilities would be hard pressed to make a go of it. Also, single men

afford more flexibility of organization—transfer, changes in location, etc. An ideal single man, however, is one who needs a job in order to support himself and whose financial house is in order. Obviously, a married man whose salary needs are moderate should also receive full consideration.

(CX 673Z–11.)

94. The record shows the following length of service distribution for respondent's field representatives at the end of 1973:

Field Representative Length of Service Group	Actual Field Reps. at Year-End	
	Number	Percent
0 ----- 1 yr	741	14.4%
1 ----- 5 yrs	1,007	19.6
5 ----- 10 yrs	1,094	21.3
10 ----- 15 yrs	768	14.9
15 ----- 20 yrs	721	14.0
20 ----- 25 yrs	481	9.3
25 ----- 30 yrs	248	4.8
30 ----- 35 yrs	61	1.2
35 ----- 40 yrs	20	.4
40 ----- over 40 yrs	4	.1
	5,145	100.0%

(RX 566V–4.) [29]

B. Functions Performed

95. The field representative's job may be roughly broken down into three main functions: the morning workup, the street investigation, and post-investigative work.

96. The morning workup involves picking up the mail containing requests for reports (Jenkins 5726; Curtis 7103–04, 7110–11), checking the files to determine whether there is already a file on the subject of the inquiry, separating inquiries by lines of business and by locations of the subjects of the reports (Jenkins 5726–27, Curtis

7103-04) and "diagnosing" reports to determine need for special handling (Jenkins 5726-27).[31]

97. The cases in a branch office and within a given line of business are separated geographically by the areas where they are to be worked and assigned to the field representatives by the supervisor (Jenkins 5726-27).

98. The field representatives list the reports assigned to them on a Form 930 identifying their cases by customer, subject of report, and type of report (Curtis 7124). Field representatives should then line up their cases geographically in order to save travel time as well as to use reference materials to identify possible sources (Jenkins 5726-28, Curtis 7130). As part of the pre-investigative work, the field representative may confer or have a "put-up"[32] with his supervisor concerning possible problems in connection with the cases to be investigated (Curtis 7105-06). [30]

99. Field representatives may be either on a "once-a-day" or a "twice-a-day" schedule. This refers to the number of times that field representatives are required to report to the office per day (Jenkins 5728-29, Curtis 7107-08). Branch managers are free to determine whether their office should be on a once-a-day or a twice-a-day system (Brothers 7374).[33]

100. The field representative's schedule for street investigation is governed by whether he is on a once-a-day or a twice-a-day schedule (Curtis 7236, Jenkins 5729). The time actually spent on the street varies and may range from 3 to 6 hours.[34]

101. After the street investigation, the field representative may make telephone calls to secure information from sources he was unable to interview or to set up appointments. Such calls may be made in the afternoon, evening or the next morning (Getz 12353, Matthews 12789, Maust 8268-69, Rawls 11056-57, Clark 4003-05, Milligan 4577, Silar 3896, Wallace 2999-3000). The field representative may also confer with his supervisors concerning [31]problems

[31] Depending on the office, certain of these tasks may be performed by clerical personnel, a supervisor or by a field representative (Jenkins 5726-27, Curtis 7110, Guse 12045-46, Case 5287).

[32] "The term 'put-up' is peculiar to the Retail Credit Company—it means literally the practice of taking matters up with (or putting them up to) another person for advice or a decision." (CX 666K).

[33] On a once-a-day schedule, the field representative in the morning initially finishes handling cases from the day before. He may make telephone calls; he discusses his cases with his supervisor if necessary, and then dictates (or types) the reports. He then receives his new cases, prepares for his work on the street, and then leaves to do the street investigation, going directly home when he finishes (Jenkins 5729). On a twice-a-day schedule, the field representative receives his cases for the day in the morning, goes out on the street to investigate, and returns in the afternoon to conclude the handling and to dictate (or type) his cases (Brothers 7373, Jenkins 5729).

[34] *E.g.*, depart office between 10:00 a.m. and 12:30 p.m., finishing between 4:00 to 4:30 p.m. (Garza 9174-75); leave office between 10:00 to 12:00, finishing street work between 3:00 to 5:00 p.m. (Tr. 12328-29); depart for street at 9:00 a.m., completing street investigations by 12:45 p.m. to 2:00 p.m. (Guse 12046-47); leave office between 11:00 to 12:00 and finishing usually at 4:00 p.m. (Hinton 9618-19). In Boston, normal departure time for street was noon with the normal workday ending at 5:00 p.m. (Hakey 1576).

encountered during the investigation (Curtis 7212–13, Brothers 7370–71). After completing the handling of the reports, the field representative dictates the reports (Curtis 7128). Some field representatives on the once-a-day schedule dictate some or all of their reports at home in the afternoon or evening (Cooke 9962–63, Guse 12047, Chambers 1934, Clark 4019, Milligan 4551). Others dictate all of them the following morning (*e.g.,* Monson 3246, Pollard 312, Silar 3896, Wallace 2999–3000, Getz 12328).

V. COMPENSATION

A. Full-Time Salaried Field Representatives

102. Field representatives are compensated by a monthly salary, overtime, a mileage allowance and, if eligible, a quarterly bonus (Case 5273).

103. Salary ranges are established for various classes of respondent's branch offices and suboffices and for various classifications of field representatives within such offices (Case 5236; RX 107J).

104. Field representatives work on a fluctuating hourly basis; their set monthly salaries cover the 40 hours in the week they work. The field representative is reimbursed at the rate of one-half of his hourly rate of pay for the hours he works overtime (Case 5273). As overtime increases, the field representative's compensation on a per hour basis of effort decreases (Case 5514–15).[35] [32]

105. Respondent does not believe there should be great amounts of overtime. Overtime claims running more than 10 hours beyond a 40-hour week are examined (Jenkins 5723).

106. A field representative is expected to produce a certain amount of revenue each month from the reports he prepares (see *infra*).

107. The revenue credit which a field representative earns is computed by multiplying the price of the report charged to respondent's customer by the number of reports at that price prepared by the field representative (Hakey 1594, Case 5279–80).[36]

108. Respondent refers to the amount the field representative is

[35] *E.g.,* if the field representative makes $600 a month, overtime would be computed as follows: divide the annual salary of $7,200 by 52 weeks and then divide that number of hours actually worked in that week; *e.g.,* 45 hours to arrive at the hourly rate of pay for the week. One-half of that hourly rate would be paid for each hour of overtime (Case 5274). In practice, this works out as follows: a field representative working a 40-hour week at the rate of $600 a month would average per hour for that week, $3.46. But if he works a 45-hour week, he would average $3.08 an hour, and would be compensated for the 5 hours overtime at the rate of $1.54 (1/2 of $3.08) per hour overtime (Case 5509–10).

[36] Whether the field representative is credited with the full price of the report charged to the customer depends on the report (Case 5281). *E.g.,* on a report priced $5.75, the field representative may receive a revenue credit of only $5.00. The remaining 75 cents would be termed "No Fee Allowed" (to the field representative) or "NFA." Respondent may use the amount designated as NFA for items such as quality control, additional

(Continued)

expected to produce as the production standard (Case 5276). The field representative has a predetermined production standard, which is a dollar amount, set on a monthly basis to cover his "expenses," which are salary, mileage,[37] overtime, and stenographic [33]charges[38] (Case 5274). The production standard fluctuates month to month with the field representative's expenses (Case 5276).

109. The production standard for a month is computed as follows: assume $600 salary and $200 for expenses for a total of $800. This is divided by the field representative's reporting standard which may be 50 percent on the dollar, resulting in a production standard or amount for that month of $1600 (Case 5276).

110. The reporting standard is a percentage varying in general from 45 percent to 60 percent (*e.g.,* RX 727W, 716M). Branch offices in different code classifications have different reporting standards (Case 5317, 5326–30). A DLU has the same reporting standard as its branch office, but the reporting standard of a suboffice may differ from that of its branch office (Case 5535–36). Within each class of office, the reporting standard increases with the length of service of the field representative at 5-year intervals (Case 5321; RX 727W, 715W, 716G).

111. The higher the reporting standard, the fewer reports a field representative has to produce. Assuming expenses are the same, a field representative with a reporting standard of .55 would have to produce fewer cases than another field representative with a reporting standard of .50 (Case 5970). [34]

112. The field representative reaches the break-even point on his production if the revenue or earnings with which he is credited match salary, other expenses, and overtime (Hakey 1593–94). If his earnings credit exceeds the break-even point, he has a gain; if they fall below, then he has a loss.

113. A field representative's "gains" and "losses" are computed as follows: for each month, the field representative's total revenue

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supervision, etc. (Case 5282). NFA, however, does not exist on all reports (Case 5283). A field representative may receive extra compensation or a surcharge in the case of some reports for performing certain services, such as taking a photograph (Case 5280).

[37] "Field representatives are reimbursed for the automobile expenses associated with their work. Automobile expenses are reimbursed by applying one standard rate per mile to miles reported by the field representative up to a certain maximum per week, and another standard rate per mile to all miles reported above that maximum per week." (RX 566 IV–2.)

E.g., 15 cents per mile for the first 125 miles a week and 8 cents per mile for mileage in excess of 125 miles for the week (id. at IV–3). This was in effect January 1973 (Case 5477).

[38] "The costs of secretarial assistance associated with preparation of reports are, in effect, charged to field representatives in the comparison of actual performance to standard. Stenographic expenses are calculated based on a standard rate applied to units of stenographic effort, and a certain number of stenographic units are associated with each type of report." (RX 566 IV–3.)

The stenographic charge per life and auto report was 44 cents in 1973 for a Code 04 office (ibid., RX 715).

credit is multiplied by the reporting standard. The product of that computation is the field representative's "dollar standard." The excess, if any, of the dollar standard over the expenses is a "gain." Conversely, if the expenses exceed the dollar standard, he has a "loss" (Case 5274).[39]

114. A field representative is generally expected to produce enough reports to meet his production standard on an annual basis and, except for factors beyond his control, on a quarterly basis (Case 5275–76, N. Smith 13225–26, Curtis 7163–64). Normally, field representatives are expected to break even in a 40-hour week (Jenkins 5841).

115. A unit supervisor is responsible for seeing to it that the field representatives under his supervision prepare enough cases to satisfy their salary and other expenses (Hakey 1587–88).

116. An experienced field representative is expected to be able to complete more reports than a new employee (Jenkins 5715).

117. Field representatives receive their normal compensation whether they meet the production standard or not (Buckley 1311–12, Wallace 3025–26, Silar 4050–51). [35]

118. In computing whether a field representative meets his production standard, he may be given credit in certain instances for absences from work and allowances for certain tasks performed in the office which reduce the time available for the preparation of reports (Case 5287; RX 107Z–105–110). These include vacation credits, illness credits, disaster credit where time is lost because of adverse weather conditions, vacation on own time,[40] and absences for jury duty (Case 5287, 5517, 5892, 5288–89, 5293, 5287–88).

119. An allowance is given for time spent in supervision, and the amount is determined by the branch manager in consultation with the person involved. The amount of credit per hour of time is the credit which would be given for working an hourly rate report in the particular office (Case 5287, 5293–94; Brothers 7477–79, 7575–76; Curtis 7108–09).

120. Trainers are similarly given an allowance for the time they spend training new field representatives. This allowance is computed on the basis of the production credit for preparing an hourly rate report (Case 5287, 5294). Trainees are also given an allowance while in training (Case 5330–31).

121. Field representatives may be given similar allowances for performing various clerical duties in the office (Case 5287).

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[39] *E.g.*, if the field representative has expenses (including salary, overtime, mileage, etc.) of $900 and his dollar standard is $1,000, he has made a gain for the month of $100 (Case 5274).

[40] Time off without pay (Case 5892).

122. The Unit Supervisor Advanced normally produces two-thirds of his salary to cover his expenses, and the remaining third is made up by the branch office because he is expected to spend roughly one-third of his time in the office supervising employees (Case 5372). He and the Claim Director Advanced receive a guaranteed bonus of 10 percent of their monthly salary irrespective of their production (Case 5303, 5527–28). [36]

123. If the field representative's earnings credit exceeds salary and expenses over a quarter, then he is eligible for a bonus in that amount up to 20 percent of his salary for the quarter (Case 5274–75; RX 566 at IV–5).[41]

124. Eligibility for a 10 percent bonus commences with 3 calendar months of employment and for the full bonus of 20 percent, after 6 months of service (RX 107Z–63–64).

125. The decrease in compensation in terms of the hourly rate as a result of overtime (Finding 104) may be offset if, as a result of extra hours worked, the field representative is able to produce extra cases entitling him to a bonus or additional bonus (Case 5552–53). Overtime, if reported, increases the ceiling for bonus (Case 5302). [37]

126. If a field representative fails to record overtime, his expenses will be less, and having less expenses to cover, he needs to work fewer cases to show a gain for the month (Case 5384). The same would be true if he were to understate his mileage (Tr. 5384–85).

127. An overgainer is a field representative who prepares a number of reports so that his production credit is greater than his expenses and the maximum bonus of 20 percent (Curtis 7175).

128. Respondent's policies for salary increases generally require (other than in a general rate increase or an increase in a per dollar standard) a demonstration on the part of the field representative of

[41] This is illustrative by the following hypothetical example:

	Month 1	*Month 2*	*Month 3*	*Total*
Earnings Credit Amount	$954	$828	$885	$2,667
Mileage Expense	(127)	(127)	(127)	(381)
Stenographic Expense	(152)	(132)	(141)	(425)
Earnings Credit Available to Cover Salary	$675	$569	$617	$1,861
Monthly Salary	610	610	610	1,830
Available for Bonus	$ 65	$(41)	$ 7	$ 31

(RX 566 IV–5.)

The "earnings credit," it should be noted, was computed by multiplying the reporting allowance or standard by total revenue credit (*e.g.*, in the case of Month 1 .505 (reporting allowance) × $1890 (revenue credit) = $954 earnings credit (RX 566 IV–4)).

his ability to produce the reports needed to cover his salary (Brown 14416–17). As a general rule, a field representative is not given a salary increase unless his average monthly gain for the preceding 6 months is at least equal to the amount of the salary increase, which would increase his production standard by the same amount (Case 5419–21, N. Smith 13267–68, Curtis 7175,[42] Jenkins 5837–38, Hakey 1740–41).

129. As a practical matter, after the salaries of respondent's field representatives reach a certain point, they hit a plateau where the salary cannot continue to rise further if Company financial standards are to be met (CX 1409).[43]

B. Regular Part-Time Field Representatives

130. Part-time field representatives are paid on a per report basis. The ratio of compensation to report charge [38]may vary by office (CX 679E; RX 107Z–56). If earnings per report do not result in the hourly minimum wage, then the Home Office brings such earnings up to the minimum rate of pay (RX 107Z–56).[44]

131. The regular part-time field representatives produce the same revenue per report as full-time salaried field representatives, but since they have a lower reporting standard, there is less reporting cost per report prepared by the part-time employees (Case 5388–89).

VI. BRANCH OFFICE FINANCES

132. In respondent's view, the Company's financial success rests largely in the hands of branch office management; the need for careful cost control at the branch office level is, therefore, considered very important (RX 107Z–80).

133. Respondent "operates its business on a budget basis." The budgets for branch offices are figured and operated on an income basis, *i.e.*, standards per dollar of income, rather than on the flat budget basis used in the case of respondent's budgets for other than branch offices (RX 107E). [39]

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[42] Exceptions may be made for reasons such as low volume of available business (Curtis 7175).

[43] In his letter of resignation, one field representative stated, "I personally passed this point some two years ago and have been literally knocking myself out every month, month in and month out, to continue to show financial gains and to make bonus money." (CX 1409).

[44] A regular part-time field representative is assigned a reporting standard, which is applied against his gross revenue produced during the month to arrive at a gross figure. From this are subtracted the reimbursable expenses incurred by the field representative such as mileage. Taxes are paid on this net income; the reimbursable expenses are added back into net income to arrive at the part-time field representative's gross income for the month (Case 5310-11). For example, a part-time field representative in one of respondent's Code 03 offices would receive .44 of every dollar produced as earnings credit. In the case of a report priced at $5, he would receive .44 of that amount. From this amount, the expense items would be deducted (Case 5323–24).

134. Before the beginning of each year, respondent determines its expected costs. These are correlated with the needed profits and expected revenue, and cost objectives are set (RX 107Z–73). The starting point in the budgeting process is the Company as a whole. The same process is then followed at the regional and branch office levels (Case 5351–52, 5502–03).

135. Such cost objectives are predetermined standards, set by respondent's Home Office for every cost item in a branch office and are formulated after input from the field (Bresnahan 560, 686). A regional cost budget is then transmitted to the Regional Vice President by the Home Office (Lieber 9038–39). This official has some flexibility in varying the overall cost objectives for different branch offices in his region provided he stays within the regional budget (Bresnahan 684–86; Lieber 9038–40).[45] Financial objectives in the region may vary from office to office (Case 5552).

136. Since cost figures are predicated on a predetermined amount of revenue, if actual revenue falls short, this may impose increased financial pressure on the branch office in the attempt to meet its objectives (Lieber 9037).

Branch Office Cost Reports

137. The Branch Office Cost Report, which is filed monthly, is a tool for determining whether the branch office has met the financial objectives set for it in its budget (see *infra*). [40]

138. The Branch Office Cost Report is a statement of the business and expenses of the branch office for the financial month.[46] This report classifies expenses in a number of major groups and compares each group with standard cost. The business for the financial month represents the total charges for all inquiries received by the office through the last business day (RX 107Z–70).

139. A cost standard, as used in the Cost Report, is the maximum amount of money available on a given cost item. All cost items are allotted a certain portion of incoming revenue. Such standards are shown in decimals which are percentages of each dollar of incoming revenue. This decimal system is referred to by respondent as the

[45] The regional budget generally has a 2 to 3 mill spread, permitting the Regional Vice President to allocate this amount among his branch offices provided that the regional "bottom line" comes out the same (Lieber 9038). *E.g.*, the Mid-West Region's budget is $8 million; $24,000 (or 3 mills of the budget) may be allocated among the region's branch offices if the Regional Vice President so desires (Lieber 9040, see also Case 5504–06).

[46] Respondent's financial month consists of 21 working days (RX 107Z–70).

"per-dollar" system of accounting. Cost standards vary by rate of office and classification of business (RX 107Z–73).[47]

140. Expenses are shown both in actual amounts and on a per-dollar basis. The gain-loss standard for each item of cost is shown for the current month and the year to date, in actual dollar amounts and on a per-dollar basis (RX 107Z–70).

141. Expected revenues and costs for the year are broken down into individual months, and monthly objectives are determined as part of the budgeting process. Monthly objectives and variations from such objectives appear on the second and third line from the bottom on the front page of the Cost Report (RX 107Z–73).

142. A gain or a loss on a given item is equal to the difference between the assigned standard and actual cost (RX 107Z–73). The important figure with respect to a branch office's financial performance is the one which shows whether it has met its overall cost objective (Bresnahan 686). [41]

143. Respondent's branch managers are instructed that their overall goal is to operate within their assigned financial objectives and to give good service. To accomplish this, the office must be properly organized so that sufficient manpower is available. The determining factor on the number of employees necessary is the revenue handled. Respondent's branch managers are instructed that "[b]y closely estimating revenue and applying the standards, a budget can be established for individual cost items and also for total cost." (RX 107Z–80).

144. A branch manager may compute his budget for a particular cost item as follows if he has an objective for a gain on the cost standard:

Example: (Establishing Postage Budget)
Rate Office: $4.60—Rate Code 02
Estimated Revenue: $35,000
Objective Gain: .003 per $

Class	*Est. Rev.*	*Per $ Std.*		*Standard*
Local	$20,000	× .018	=	$ 360
DLU	5,000	× .026	=	130
Sub-office	10,000	× .035	=	350
				$ 840

[47] Classification of business means that all incoming revenue is classified in one of the following categories such as local (*i.e.*, within the branch office), suboffice or DLU. This classification depends primarily on the location of the field representative producing the revenue (RX 107Z–73).

Est. Rev.	*Per $ Gain*		*Obj. Gain*
$35,000	× .003	=	$ 105

Standard	*Obj. Gain*		*Budget*
$ 840	- $ 105	=	$ 735

i.e. The office will meet its objective postage gain of .003 per dollar provided the office handles $35,000 revenue and operates within the budget of $735.

(RX 107Z-80.) [42]

145. Reporting cost is the branch office's major cost item (RX 107Z-84). It includes the field representative's salary, overtime, carfare, gains or losses on reporting standard, as well as charges and credits for supervision and training (RX 107Z-71). Field representative losses are charged against the branch office (Case 5519).

146. Training costs can drain branch office finances if there is extensive and heavy training over a short period of time (Eldred 11302). And, if training costs become unexpectedly high, it may be difficult to stay within branch office financial objectives (Lieber 9125).

147. Respondent's system of setting cost objectives for its branch offices necessarily limits the resources available for training and supervision in the field[48] and thus, the branch manager's discretion in this area. [43]

148. The Cost Report also includes detailed work records for all salaried field representatives and a comparison of the total expense incurred by each field representative with his reporting standard (RX 107Z-70). In the context of the Cost Report, the reporting

[48] *E.g.*,

> Frankly, the Home Office has not yet set in concrete your final cost objective for the year; although when the objectives were sent out about a month ago, this was the original intent. However, we have raised such a clamor from the regions that there has been agreement that some further considerations will be given to certain office situations, and your office was one of them.
> *I have recommended that your office be raised from .724 to .727 or .003.* This does not seem much, but it is better than the original figure that was spewed out by the computer.
> In view of the fact that the objectives have not been finalized, there will still be further adjustments during the month of June; therefore, we do not know exactly where you or the other offices stand on the accumulative variations, etc. *It is too early to become too upset with what happened in May until every cost objective and all adjustments have been finalized for the year.*
> *Until then, sit tight and do everything you can humanly do to hold costs to the bare minimum as there will not be any monies for some of the things we would like to have, such as more money for supervision, training,* etc. Such a large portion of the additional money available from the increase went to employees that *there is just not much left to provide the branch with a great amount of leeway for the remainder of 1974.*
> As soon as I get further word in regard to your objectives for the remainder of the year, I will let you know.
>
> (Regional Vice President to Manager, Albuquerque office, June 21, 1974, CX 813; emphasis supplied).

standard for salaried field representatives is based on a percent of revenues handled. This standard provides for all expenses incurred by the field representative including salary, overtime, car expense, stenographic cost (RX 107Z–73).

149. Gains on the reporting standards are added into the reporting cost figures for the financial month and are set up in a reserve for payment of bonus each quarter.[49] The reporting standard for field representatives varies by length of service and location (RX 107Z–73). [44]

150. The Branch Office Manager's Manual states in connection with the control of field representative work:

Control of Field Representative Work: The Field Representative's work should be controlled by the Manager from two standpoints. First, to see that the number of reports each Field Representative makes is limited to his experience and ability. Second, to see that each Field Representative makes enough reports to show a gain on reporting standards after his three-month training period; and that during the training period, his loss on reporting standards will not exceed the training allowance.

(RX 107Z–80.)

151. Accumulative field representative losses and field representative losses made up are to be considered together on the branch cost report since they are respectively treated as charges and credits to the branch office (RX 107Z–115). In short, where the field representatives of a branch office accumulate a loss, that loss is charged to the branch office as part of the cost of operating that office (Bresnahan 571).

152. Where training costs exceed the applicable cost standard, this is shown as a loss to the branch office (RX 107Z–84, 95) [50] [45]

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[49] A field representative's gain-loss on his cost standard for purposes of the cost report may be computed; *e.g.*, assume the following:

Business for the month produced by field representative	$1613
A per dollar standard of	.525
Expenses of $674	

Multiplying the per dollar standard of .525 times his business produced of $1613 gives a per dollar standard of $847 in dollars.

Subtracting actual expenses of $674 from $847 shows this field representative has made a gain on his cost standard of $173. (Case 5377–78; RX 673Z–107).

[50] The training allowance for all new field representatives for the first 12 weeks was $525 in 1973, broken down as follows:

Week	*21 Day Month*
1st	147
2nd	86
3rd	69
4th	52
5th	42
6th	34
7th	29
8th	19

(Continued)

153. Individual field representative losses are carried forward until the losses are made up by the field representative or other management action is taken. When a field representative transfers from one office to another, his losses are dropped in all instances. Field representatives transferring within a branch continue to carry their losses until they are made up. Field representative losses are carried forward into any number of months and quarters until they are made up (RX 107Z–115). As a general rule, no gains by a field representative are carried from one quarter to the next; but if gains are carried, they are carried over in the unit bonus pool and not by the individual field representative (RX 107Z–64).[51]

154. As a general rule, a field representative should gain on the reporting standard before being paid bonus. And:

> A Field Representative is not eligible to receive bonus until losses are made up by subsequent gains. Any exception to this requires a complete put-up to the Regional Vice President-Operating. If he approves, he will forward the request to the Home Office for final approval.

(RX 107Z–64.)

155. Since exceptions to the general rule require consultation with the Regional Vice President-Operating and final approval by the Home Office, the award of a bonus to a field representative carrying losses is an unusual occurrence. [46]

156. It is the branch office manager's responsibility to meet or do better than the cost standards applicable to his office (Bresnahan 562).

157. If a branch office manager did not meet his financial objectives for the year, it affected his bonus adversely. If, in addition, his performance was questioned in other areas, such as personnel management or quality service, then his capacity to manage the office may have been brought into question (Lieber 9144).

VII. REPRESENTATION OF IDENTITY BY RETAIL FIELD REPRESENTATIVES (PARAGRAPHS 5–6 OF THE COMPLAINT)

158. Respondent's 1973 Field Representative Manual instructed

9th		17
10th		11
11th		11
12th		8
13th—17th		—
	Total	525

(Rates and Financial Guides United States Effective March 1973, RX 715Z–1).

[51] One of respondent's officials testified, however. that the branch manager had discretion to give such credit in the next quarter to the same field representative who earned the excess bonus (Case 5296).

the field representative to state his name and Retail Credit's name when interviewing the subject of a report (RX 102Z–4).[52] The field representative was permitted to mention the name of the company requesting the report and was encouraged to do so.[53] In interviews of sources other than the subject of the report, neither the name of Retail nor the requesting company was required to be given (RX 102Z–11). In both instances, the manual pointed out that the field representative should never misrepresent his identity (RX 102 Z–11) and that he was to avoid "any impression that [he was] employed by the insurance company" (RX 102Z–4). [47]

159. Prior to the 1973 amendments, the Field Representative Manual stated that the name Retail Credit should be used when interviewing the subject of a report. However, it also suggested that when the requesting company desired use of its name in the introduction, then "the Field Representative should state that he is 'calling for the X Insurance Company' " (CX 666Z–4).[54]

160. Respondent's name, Retail Credit Company, sometimes confused consumers and led to the impression that credit rather than insurance was the reason for the investigation (CX 666Z–4, 666Z–10; Stubbs 9293). Respondent recognized this fact and instructed field representatives to explain Retail's "role in the insurance field" when confusion occurred (RX 102Z–4, see also RX 102Z–11).

161. In practice, the name Retail Credit was not always used in the field representatives' introductions even in interviews with subjects of reports (CX 748, 1243A; Jenckes 98–99, Hakey 1633–34, Dodson 3072–73, Feriante 4441, Pollard 321–22, Boyd 13156–57). Many field representatives did not identify themselves as employees of Retail because they did not want to become involved in explaining Retail's business.

> The assumption people made, I was making some type of credit report because of the name Retail Credit Company, and usually it involved, or my experience was that it involved an explanation of what a credit company is doing here. As a result, by introducing myself as an insurance inspector and not by contradicting myself by saying I am from what they consider to be a credit company or loan company, it would save me a lot of hassle, and of course when you are on the road, time is of essence. (Hakey 1634–35; see also Dodson 3072–73, Pollard 321). [48]

162. Consumers were told by the field representatives contacting them that they were "from", "with" or calling "for" the insurance

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[52] Field representatives were issued Retail ID cards, but the corporate instructions did not require that they be produced at interviews (RX 102Z–4; see also Jenkins 5852–54).

[53] "It is not necessary to volunteer the name of the requesting company unless this information is asked by the subject. But, doing so in most instances should facilitate the interview." (RX 102Z–4).

[54] While the manual drew a distinction between saying the field representative was calling "for X Insurance Company" and "from X Insurance Company," either introduction would misrepresent, by implication, the identity of the caller if Retail Credit were not mentioned (see Finding 163).

company or other customer of respondent (who had requested the report), that the interviewer was "conducting an investigation for" the insurance company or that the interview was in connection with a particular insurance application (Epperson 3939, *in camera*; Luster 3167, 3179; T. Gracey 1889, 1891–92; CX 1448A–B; McCreary 1860;[55] Hall 1909; Grabher 3412, 3416–17, 3420; E. Sattler 4269; Baker 3108). The field representative contacting consumer Byers stated his identity without mentioning Retail Credit and questioned her regarding her automobile and automobile insurance for which she recently applied. Ms. Byers formed the impression that he was from the insurance company (Byers 4472–73, 4476).[56]

163. An introduction by a field representative stating that he was "from" or making contact "for" an insurance company, that he was calling in connection with an insurance application or a similar introduction unaccompanied by the disclosure that he worked for Retail, had the tendency to create the impression that the field representative was an insurance company employee or agent rather than the employee of a third party consumer reporting agency. [49]

164. Whether an interviewer was an employee of a company with which the consumer or subject of the report had already established a relationship (such as an insurance company) or an employee of Retail, was a significant fact to a consumer being interviewed in determining whether to furnish the information requested. Some consumers who discovered that the interviewers were actually employees of Retail refused to continue with the interview or answer any more questions (Hall 1910–11, McCreary 1863). When consumer Sattler discovered the field representative was a Retail employee, he felt the introduction had been "misleading and deceptive" (E. Sattler 4270). Consumer Byers was not sure she would have answered the questions asked her had she known the true identity of her interviewer (Byers 4474, 4476–77).

165. Inherent in the belief that the interviewer is an employee or agent of the insurance company, or other requesting organization, is the belief that information provided during the interview will be used exclusively by the requesting company. In fact, respondent keeps a file copy of each report its field representatives prepare, and

[55] Consumers Gracey and McCreary were interviewed in connection with a survey of people on municipal disability retirement requested by the City of Miami (Tr. 6562–A–B). A Retail memorandum states that the city requested "that the inspector is to tell the claimant that he is calling in behalf of the City of Miami Welfare and Pension Department, during the interview." (RX 486C).

[56] The witnesses testifying in rebuttal to the testimony of consumer Hall did not dispute the portion of her testimony on which this finding is based. The testimony of consumers Epperson, Grabher, Sattler and Byers was not outweighed by the rebuttal witnesses called, the field representatives who contacted the consumers. These witnesses did not testify regarding the particular contacts in question, but rather related the introductions they generally used (Tr. 12080–81, 11741–42, 11152–53).

these file copies may be used in subsequent reports prepared on the same consumer (CX 666K–O; RX 102I–J). Field representatives do not affirmatively state or volunteer in an interview that respondent keeps file copies of its reports (Pollard 322, Boyd 13175–76, Hakey 1634). Respondent's field representatives, by misrepresenting their identities, also misrepresent the use to be made of the information obtained during an interview.[57]

166. By its field representatives' misrepresentations of identity, respondent violated Section 5 of the FTC Act. [50]

VIII. REPRESENTATION OF PURPOSE BY RETAIL FIELD REPRESENTATIVES (PARAGRAPHS 7–8 OF THE COMPLAINT)

167. Since 1966, respondent has used the "indirect approach" in its interviews with third-party claimants on whom claim reports are being prepared (RX 651A). As defined and set forth in the 1966 Claim Reports Manual, the indirect approach involved the following:

Method Used on the Indirect Approach: The accepted and sanctioned approach is for the Inspector to give the name "Retail Credit Company" and indicate that he is making inquiry, ostensibly for credit purposes. To help the investigator validate his position, he is supplied with a form described as the Credit File Audit, Form 4958, which permits him to record pertinent data without arousing suspicion. If the claimant is supposed to be disabled, the credit put-up enables the investigator to ask whether he has been working steadily, whether he has had any recent heavy expense which might come from illness or injuries, and other questions which will lead into a discussion of activities, background, and claim or medical history.

(RX 651A.)

168. The Credit File Audit procedure instituted in 1966, supplanted Retail's previous procedure for interviewing third-party claimants—the "pretext" interview, which had been used for many years (Stubbs 9257–58).[58] [51]Mr. Trotochaud, who wrote the 1966 indirect approach amendments to the Claim Reports Manual, explained the change:

Over a period of many years, our instructions provided that in the handling of claim investigations on third party claimants, we would use a suitable pretext, but the

[57] This finding of misrepresentation as to the use of information is based on the finding of misrepresentation of identity by field representatives, rather than solely on respondent's failure to affirmatively disclose to consumers that it keeps a file copy and may subsequently use it. The record permits no finding as to what a consumer would believe regarding the use of information, if he were aware that the interview was being conducted by a Retail employee.

[58] In addition to its use in claim reporting, the pretext interview was used in some work other than claims, *e.g.*, attempting to locate individuals for failure to pay on credit cards, or attempting to locate uninsured motorists (Jenckes 78–79).

instructions did not go beyond that. So, therefore, the field representative was left on his own as to how he would proceed.[59]

I felt strongly that this was not a proper procedure and had made up my mind that, given an opportunity, I would correct that to lay out clearly and completely how he should approach an investigation on a third party claimant.

I was given that opportunity, and this claim reports manual was written in 1966. I wrote it and at that time implemented instructions that they would handle these investigations on what we termed an indirect approach basis. And that indirect approach basis was spelled out, and it stated that the field representative must, must, in every instance, identify himself as being with the Retail Credit Company. (Trotochaud 6347; footnote added).

169. Though the 1966 revision was intended to result in deletion of the term "pretext" from the vocabulary of Retail personnel, many employees used the term pretext interview in connection with the Credit File Audit interview (Bresnahan 612–13, see also Buckley 1261–62).[60] [52]

170. The Credit File Audit Interview form used by respondent in the indirect interview was the following:

RETAIL CREDIT COMPANY

CREDIT FILE AUDIT

DATE _____ FILE NO _____

AUDITOR: We are attempting to confirm that our files are correct on this individual. Conduct a direct interview with the subject or an adult member of the family.

NAME _____ AGE _____

ADDRESS _____

FORMER ADDRESSES (if any) _____

PRESENT OR LAST KNOWN EMPLOYMENT _____

_____

PRESENT OR LAST KNOWN JOB TITLE _____

NOTE: IF PRESENTLY UNEMPLOYED, WHAT IS REASON? CHECK ONE:

TEMPORARY LAY OFF __ SICKNESS OR ACCIDENT __ OTHER REASON __

LENGTH OF TIME OFF WORK _____ OTHER INCOME _____

NUMBER OF DEPENDENTS NAME AGE

(include name and age) _____ _____

[59] As an example of a pretext used, one field representative stated, "I would go the claimant's home and say that I was looking for a person I believe that resided in the neighborhood, and had they ever heard of that person." (Jenckes 77–78).

[60] As late as 1972, respondent was still engaged in purging the term "pretext" from its reports (CX 1323A).

_____ _____

_____ _____

HOME OWNER..... YES _____ NO _____

CAR OWNER..... YES _____ NO _____ (MAKE AND MODEL) _____

IS SPOUSE EMPLOYED, IF SO, WHERE: _____

AUDITOR: Make any notes here to clarify any of the above questions.

Form 4958-9-60
Printed in U.S.A.

(RX 651B.) [53]

171. The primary purpose of direct contact with a claimant is to observe the physical condition of the consumer (Jenckes 77; RX 119Y-Z; CX 1323D; Murray 9572).

172. The Credit File Audit form was designed so that when seen by the interviewee (Stubbs 9259, Trotochaud 6348), it would give the impression that the investigation being conducted was a credit investigation (Bresnahan 700-01). The information recorded on the form could be useful to Retail in its claim report (*e.g.*, the form contained a blank for unemployment due to illness). However, the basic purpose of the form evidently was to create the impression that the reason for the field representative's visit was to conduct a credit interview.

173. Respondent's name made the representations concerning the ostensible subject of the indirect interview more convincing since "Retail Credit" connoted credit to consumers (Finding 160).

174. Respondent's rationale for pretext, and later indirect, interviews was as follows:

> The person claiming is not their insured, it is a third party, maybe there's a lawyer in the picture, maybe there isn't, but that person is making a specific claim that they need to know the background on, and in so many instances the cooperation in getting medical to them and full details has not been the best, and just generally a person in that situation, if you went up to them, a person who is claiming a whiplash injury and say I am here from the X insurance company to question you about your whiplash, are you working anywhere, are you still playing golf, or so forth, it just wouldn't be—if that person had anything speculative on his or her mind it would not be in the interests of that person considering what they are trying to do to say yes, I am working the midnight shift somewhere, or play golf three times a week, this is basically the background of that. (Stubbs 9253).

[54]In short, with the pretext or indirect interview, "You would acquire information that you might not normally acquire." (Bresnahan 615).

175. The Credit File Audit indirect approach had the capacity to

mislead consumers as to the purpose of interviews. This procedure was unfair and deceptive within the meaning of Section 5 of the FTCA.

176. In 1971, respondent modified its indirect approach procedure and abolished the Credit File Audit interview (RX 575A–C; Trotochaud 6355). Under the new procedure, the field representative was instructed to state only his name and that he was from Retail Credit. He was to complete a "Personal Interview" form (RX 575C) which was essentially the same as the Credit File Audit form but contained the title "Personal Interview." Like the Credit File Audit form, the Personal Interview form was designed to be seen by the claimant, and field representatives were instructed that they could "even let the individual personally handle the form if he [were] so inclined." (RX 119V). If the field representative were asked the purpose of the interview, he was to state that he was not permitted to divulge the purpose or the source of the request (RX 575A). The new procedure, as codified in the 1973 manual, was as follows:

> . . . The accepted and sanctioned approach is for the Field Representative to give the name 'Retail Credit Company'. To help the investigator validate his position, he is supplied with a form described as the Personal Interview, Form 4958, which permits him to record pertinent data. If the claimant is supposed to be disabled, this put-up enables the investigator to ask whether he has been working steadily, whether he has had any recent heavy expense which might come from illness or injuries, and other questions which will lead into a discussion of activities, background, and claim or medical history.

(RX 652A.) [55]

177. Field representatives were later instructed to use this indirect approach in all claim or loss investigations unless the requesting company had given specific authorization to the contrary (RX 653A). Respondent's policy favoring indirect interviews was so strong that when the Regional Claims Manager discovered that a branch office manager had permitted his claim field representatives to use the direct approach instead, he "very strongly suggested" that the indirect approach be used (Stubbs 9256).

178. The field representative's instructions in 1971, stated that, *"It is imperative that our approach not include any misrepresentation"* (RX 575A, emphasis in original), and field representatives were told not to affirmatively state the purpose of their interview. However, the indirect interview approach itself, providing for use of the Personal Interview form, had the capacity to mislead consumers as to the purpose of the interview and to lead them to the belief that credit was being investigated (Murray 9596–97). That respondent intended that consumers be led to believe the interview was for

336-345 O - 81 - 57

credit purposes is shown by the fact that, in contrast to the direct interview instructions (Finding 160), the indirect interview procedure did not include a requirement that field representatives clarify any confusion created by the name Retail Credit (Edland 11759).

179. Respondent's 1971 modifications of the indirect interview did not cure the deception inherent in the pretext and Credit File Audit interviews. The "Personal Interview" format, while not involving affirmative misrepresentations, had a tendency to create the same impression as did the Credit File Audit. Like the Credit File Audit, this approach, when used in conjunction with Retail's name, was likely to lead the consumer to believe the purpose of the interview was to obtain credit information, rather than data about the [56]health and activities of a claimant in an insurance claim.[61]

180. Respondent's indirect interview procedure has the capacity to mislead and is unfair and deceptive within the meaning of Section 5 of the FTCA.

181. While respondent engaged in unfair practices within the meaning of Section 5 of the FTCA (Findings 175, 180), such practices were engaged in as part of the business of insurance and, therefore, are exempt from regulation by the Federal Trade Commission to the extent that they are regulated by state law.

IX. ALLEGATIONS THAT RESPONDENT HAS MISREPRESENTED THE MANNER IN WHICH ITS REPORTS ARE PREPARED (PARAGRAPHS 9–10 OF THE COMPLAINT)

A. Use of the Telephone in Interviewing

182. Respondent's procedures for interviewing and securing information vary depending on the report involved.

183. Certain of respondent's reports are designed and intended to be handled by one or more telephone interviews (Jenkins 5776). *E.g.*, various types of automobile classification check reports are to be handled primarily or exclusively through telephone interviews and the instructions on the form so state (Moore 8854, Jones 12953, Lindgren 11456, Mayo 10752–53, L. Jones 10440, Rawls 11059, Saltzgaber 11967, Getz 12345, J. Moss 11033–34, Hakey 1581–84). In the case of these reports, the extent to which the telephone is used may be specified by the customers (Hopp 6691–92, [57]Zack 8257). Certain credit line reports and some employment reports are also

[61] Complaint counsel offered three consumer witnesses to support the allegations of paragraphs 7 and 8 of the complaint. The testimony of these witnesses contained facts showing departures from respondent's established procedures. There is no need to make findings on the testimony of these witnesses in light of the finding that respondent's established procedures themselves were misleading.

handled by telephone (Knautz 6881–82, 6896–97; Chambers 1957; Hille 4526).

184. Use of the telephone in the case of claim reports is limited, and violation of such rules results in dismissal (Trotochaud 6310). When the telephone is used in preparation of claim reports, its use must be shown on the report (Trotochaud 6309–10).

185. In the case of the majority of the reports made by respondent, such as life and health reports, regular automobile reports, property reports and most personnel reports, the telephone is used to some extent (Jenkins 5776, Lieber 8998).

186. In the case of these reports, it is respondent's basic policy that telephone use has been "limited to the degree that you can limit it and good judgment dictates" (Jenkins 5776–77). Some telephone use is permitted in the case of these reports because "[f]or limited price reports we cannot obviously make repetitive return trips" (Tr. 5777).

187. Managers and supervisors have discretion when to permit use of the telephone in the preparation of such reports (Jenkins 5777). Respondent has no written guidelines on use of the telephone in specific situations because this might interfere with the exercise of discretion and judgment on this question at the branch office level (Browning 6074–75).[62]

188. Branch offices authorized telephone contact for specific classes of sources under certain conditions, *e.g.,* the applicant's employer (Hilderbrand 12006, Jones 10440–41, Martin 10512). Telephone interviews could also be used with professional persons such as attorneys whose schedules might not permit in-person interviews (Garza 9163–64, Jones 10441, Mayo 10753). [58]

189. Certain branch offices permitted use of the telephone to interview managers of apartment complexes who requested telephone contacts (C. Hood 6498–99, Larson 12518, Guse 12063); in obtaining public or school record information (Volrath 11001); in setting up appointments for face-to-face interviews (Brothers 7406, A. Brown 7742–43, E. Jones 12923, J. Moss 11037–38, Cain 9464, Nazarchyk 8032, Tew 13368–73); in locating the residences of subjects or sources in rural areas (Brothers 7406, Cain 9464); when bad weather conditions prevented street investigation (Horner 9887–88); when speed was required due to an insurance company's request for expedited handling (Getz 12345); where applicants or sources were outside of, or about to leave, the area (Larson 12545); when evening contacts were required (A. Brown 7743–44, Zack 8216); when

[62] It is respondent's position "that first line supervision must concur when a telephone is used to meet the logical source . . .". ." (Browning 6075).

a source or subject could only be reached by telephone (Browning 6077, Landreth 12133); or when a direct interview with the applicant was required to obtain necessary information (Browning 6076, Zack 8216–17).

190. The general policy in effect in most branch offices on reports not specifically designed for telephone handling was that field representatives had first to make a reasonable effort to handle the case on the street by attempting to obtain face-to-face interviews but that the telephone could be used if such attempts were unsuccessful (*e.g.,* Vogen 12202–03, Volrath 11000–01, Dodson 3054). First-line supervision was to concur when the telephone was used for that purpose (n. 62, *supra*).

191. It was the responsibility of the branch office manager to exercise supervision enabling him to determine whether use of the telephone had been excessive (Lieber 8999).

192. Use of the telephone had increased significantly because of social and economic changes occurring in the 1960's and 1970's. Such factors include the greater frequency of both spouses working during the day (Coleman 7923–24, Ross 9349), the increase in apartment complexes (Jenkins 5730–31) and increasing danger to the physical safety of field representatives in certain urban areas (Murray 9574, Laugavitz 10334–35). [59]

193. The objective in preparing reports was to obtain face-to-face interviews with applicants and outside sources whenever possible (*e.g.,* Brothers 7406, Vogen 12203, Ross 9348).

194. Field representatives were instructed to so indicate on respondent's file copy of the report after identification of the source when the interview had been conducted by telephone (*e.g.,* Baranek 9697–98, Coleman 7925, Moore 10046–47). Respondent did not normally place a notation that the telephone had been used in its underwriting reports going to customers (Jenkins 5777–78,[63] Browning 6077).

195. There was a requirement, however, that customers be specifically notified of telephone use on intermediate, special narrative and special life reports (Crepeau 1756, Ledum 4683, Curtis 7137, Lauer 10155–56, M. Martin 10512).

196. In addition, telephone use was shown on the customer's copy of the report if the customer had made a request to that effect (Browning 6077). And, in certain branch offices, a decision was made locally to indicate telephone handling on the customer copy (*e.g.,* Eldred 11221, Saltzgaber 11990).

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[63] "[W]e have always taken the position on underwriting reports that we sell information and not systems" (Jenkins 5778).

197. In respondent's "Pro Series Life" reports introduced in 1976, all reports in the series showed whether the interview was conducted "in person" or "by telephone" (Stansbury 6821–22, 6826). Respondent was informed by customers that:

it would be helpful to them to know how the information was obtained. [60]When they evaluate the information and handle it with their field forces or within their own organization, they have a better idea about it, based on knowing how it was obtained. (Stansbury 6821–22).[64]

B. Respondent's Representations Regarding Face-To-Face Interviews and Personal Observations Made by Field Representatives In the Preparation of Reports

198. Respondent's customers were told that normally respondent attempted to obtain information in person but that, if necessary, the telephone was used to interview applicants and outside sources (Drennan 6218, Vogen 12214).

199. Respondent, in its brochures to customers, has represented:

(a) You see your applicants even though you aren't able to visit each one yourself. Retail Credit Company's Hospitalization Interview Service is the next best thing to being there. This service affords you an in-depth view of your applicant, his living conditions and answers to such health and environment questions as:

- Is he impaired?
- Overweight?
- When did he last visit a physician?
- Hazards in the household?
- Are living conditions sanitary?
- Does he live in crime and vice area?
- Plus much more . . . (CX 384B.)

(Brochure entitled, "The Next Best Thing To Being There", CX 384A–D). [61]

[64] Such customers, while they "were not concerned or are not concerned overall" whether the telephone was used did want to be informed of such use so "they [would] have a better idea about it" (ibid).

(b) HEALTH HABITS: He presents a normal, healthy appearance. He is not impaired or handicapped . . . .

(Quotation from specimen, "PERSONNEL SELECTION INVESTIGATION" report in promotional brochure, "a crucial moment in any training operation", CX 386A–B).

(c) The best method of obtaining business and marketing information is through personal interviews or by direct observation . . . .

(Brochure entitled, "RETAIL CREDIT COMPANY EXECUTIVE REFERENCE MANUAL a straight line to facts about people for better business decisions", CX 387M).

(d) He (the investigator) checks files and public records. He then performs an on-the-street investigation interviewing logical sources for the information needed. These are usually neighbors and business associates and sometimes the applicant himself. A report is written and sent to the underwriter.

(Brochure entitled, "LOOK TO THE FUTURE", CX 389E).

(e) It [Retail Credit's Life & Health Insurance Service] is based on an interview with the applicant as the primary source of information, allowing for an in-depth interview of the applicant. It helps to:
- Establish age and identity
- *Observe the applicant's physical appearance and environment*

(Brochure entitled, "88% personally interviewed," CX 398A–B; emphasis supplied). [62]

(f) We have found the most dependable reporting method, for whatever purpose, is the personal interview . . .

When field representatives call personally on these logical sources, they introduce themselves as representatives of Retail Credit Company . . . .

(Brochure entitled, "THE WHY AND THE HOW", CX 399N; emphasis supplied).

200. Respondent, in its brochures to prospective users of its reports, through language such as: "the next best thing to being there" and "[y]ou see your applicants even though you aren't able to visit each one yourself . . . [t]his service affords you an in-depth view of your applicant, his living conditions and answers to such health and environmental questions as: Is he impaired? Overweight?" and similar language has represented that, as a matter of standard procedure, its reports are compiled through face-to-face interviews

with the sources listed and upon the basis of the direct observation of the field representative making the report.[65]

201. Entries on report forms such as:

Is there anything unhealthy about appearance, such as being very thin or having excess weight?
Any deformity, amputation, blindness, deafness, or other defects?

(CX 422A.) [63]
also impliedly represented that the field representative who supplied such information had observed the subject of the report.

202. The inspection report is one of the more important documents that an underwriter uses in evaluating an insurance risk (Hartzler 801).

203. Certain underwriters assumed residential sources were usually interviewed face-to-face (Davison 2634–35, 2676).

204. If a life report indicated that the applicant was interviewed, certain users of reports construed this as meaning that there had been a face-to-face interview (Hartzler 826).

205. If a report contained information as to an applicant's physical appearance, underwriters expected that such information was obtained through direct observation (Snore 3658, Davison 2638).

206. Certain underwriters believe in-person interviews are more reliable than telephone interviews (Hartzler 826, 873; Davison 2637).[66]

207. Certain underwriters expected to be informed that the telephone was used to interview an applicant or a neighbor when the source was interviewed in that manner (Snore 2655–56). Certain users of respondent's reports believe that knowledge as to whether a source was interviewed by the telephone or in person is important in determining how much confidence to place in the information reported (Nietzhold 13045, Dower 2142). [64]

208. Some underwriters do not care whether the telephone is utilized on a case small enough to require only a regular report (Paine 13439–40).[67] In the larger cases, however, even these underwriters would place greater reliance on or prefer a face-to-face

[65] Respondent urges there is no testimony that any underwriter has read or relied on its promotional literature (RPF 186). There is, however, a presumption when brochures of this nature are prepared and disseminated, that the intention is that they be relied upon.

[66] A number of respondent's employees also preferred in-person interviews (Baranek 9717–18, Cooke 9981, Brothers 7482, Hartfield 10497, L. Jones 10472, M. Martin 10542, Muth 9948, Pregler 9210, Crofford 8118, Garcia 13133–35). That preference is generally based on the fact that in-person interviews allow them to observe the physical appearance of the applicant (L. Jones 10472, Muth 9948, Zack 8927, J. Curtis 7249); or his or her demeanor and expressions in responding to questions (Baranek 9717–18, Muth 9948); or, occasionally, the interior living conditions of the applicant's residence (Ross 9348, Brothers 7483).

[67] In such small cases, such underwriters would not put a different degree of reliance on information received by telephone as opposed to a face-to-face interview (Paine 13439–40).

interview because of the opportunity for direct observation (Paine 13406–07; Taylor 10860–61, 10881–82).

209. The preference for face-to-face interviews on the part of such users in the higher-priced cases compels the inference that the "how" of preparing a report viz., telephone as opposed to face-to-face contact, does significantly affect the manner in which report information is evaluated. The reason that it is a matter of indifference to some report users in the case of lower priced reports is inherently economic.[68]

210. If the inspection report contained adverse information pertaining to the applicant's home or physical surroundings, certain underwriters expected the field representative to have physically observed them (Snore 3659–60, Davison 2638–39).

211. Certain of respondent's field representatives have reported information concerning the appearance of the subject of the report or his home or physical surroundings, when they did not personally observe the subject of the report or his physical surroundings (Buckley 1349, Dodson 3064, Hakey 1560, Woicik 2874–75, Wallace 3004–06).[69] **[65]**

212. Information derived from telephone interviews concerning physical appearance and physical environment may be accurate even though the telephone is used; sometimes such information can be cross-checked with other sources (*e.g.*, Stansbury 6751–52). But this is not the optimal method. As one insurance company executive testified:

> Q. Isn't this information [the build of an individual] that might be best obtained by personal observation of the insurance applicant rather than by talking with the insurance applicant over the telephone?
>
> A. Yes, personal observation would be of more merit than a telephone conversation. It would be difficult to obtain someone's build by phone. (Taylor 10860–61).

213. The manner in which interviews are conducted; namely, telephone or face-to-face, is a significant factor in evaluating consumer investigative reports.[70] **[66]**

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[68] "On a small case, frankly, we can't afford it. We can't pay for that" (Paine 13407).

[69] Even assuming that a field representative was familiar with the living conditions in the area in which he prepared reports, such general familiarity with a neighborhood is no substitute for direct observation of the particular physical surroundings of the specific individual being reported on. *E.g.*, one report asked, "Premises poorly kept?" (CX 477A). Generalizations about the neighborhood "would not necessarily apply to the applicant's own dwelling or his own individual living conditions" (Stansbury 6753).

[70] This finding is compelled by the following: respondent's brochures represented that personal observation is the standard procedure (Finding 200). Branch office managers are to determine whether telephone use is excessive (Finding 191). Telephone use is to be noted on respondent's file copies (Finding 194) and telephone contact is to be noted on the customer copy of the more expensive reports such as intermediate special narrative and special life reports (Finding 195) Respondent, in 1976, commenced showing on all reports in the Pro Life Series whether the telephone had been used because "Customers told us . . . it would be helpful" and because respondent's customers felt "when they evaluate the information they have a better idea about it based on knowing how it was obtained"

(Continued)

214. The failure to indicate on the customer's copy of the report that the telephone had been used when a source had been interviewed in that manner constituted the failure to state a material fact and was misleading.[71]

215. The failure to disclose that descriptions of the appearance of a subject or his physical surroundings had been obtained from other than by personal observation, *e.g.*, by telephone or general knowledge of the area, also constituted the failure to disclose a material fact in violation of Section 5 of the FTCA.

C. Dissemination of Reports Listing Sources Not Interviewed

216. The listing of a source on a report represents that that source has actually been interviewed (*e.g.*, see Question 3 on CX 422). Some report users give more credence to reports where information contained therein is based on more than one source (Dower 2141). It was the expectation of report users that all the sources listed in a report were, in fact, interviewed by field representatives who prepared such reports (Davison 2686). If fewer sources were interviewed than listed on the report, this necessarily detracted from the confidence to be placed in the report.

217. Certain field representatives listed sources not contacted in reports which they filed (see Finding 405). To the extent that reports listing sources not interviewed have been sold, the users thereof have been misled as to the accuracy of the report. [67]

X. ALLEGATIONS CONCERNING RESPONDENT'S USE OF CERTAIN AUTHORIZATIONS TO SECURE MEDICAL INFORMATION AND ITS SUBSEQUENT USE OF SUCH INFORMATION (PARAGRAPHS 11, 12, 13 OF THE COMPLAINT)

A. Nature of Medical Information

218. Medical information on a given consumer may appear in either hospital or physicians' records. Such records show the diagnosis, treatment and progress of the patient (Pheasant 11391).

219. Medical records may include laboratory and x-ray results and findings of consultant physicians (Pheasant 11399). The records should include objective findings and clear reasoning as to why a diagnosis was chosen or a certain treatment selected (Gabrieli 1400).

(Finding 197). Even those underwriters who do not care whether the telephone is used in lower priced reports of necessity must be deemed to place greater reliance on information derived from face-to-face interviews in view of their preference for this method of investigation when the economic risk is higher (Finding 209).

[71] This does not apply to those reports which were designed for telephone handling and sold on that understanding.

They may also contain information about the patient's habits (Gabrieli 1401), his emotional or physical activities and condition (Elmendorf 4247A, Pheasant 11396), or psychiatric condition (Gabrieli 1402–03). A psychiatric record gives a history of the patient's lifetime pattern, including not only his symptoms but also his ideas, dreams, and thought processes. It may include correspondence, information received from and about his family and other people, and the patient's experiences (Grossman 4168–69). Other medical records may also include such psychiatric information, since many symptoms and illnesses have an emotional basis (Grossman 4173–74). In addition, medical records may contain the subjective impressions and opinions of the physician on matters such as the honesty of the patient (in relation to revealing matters such as alcoholism or sexual problems), or his level of intelligence (Gabrieli 1400-02, Grossman 4175–77).

220. Medical records are maintained for the benefit of the patient. They identify his problems and what treatment he has had, to provide continuity of care (Elmendorf 4247, Grossman 4174–75, Pheasant 11391). In addition, such records may be kept for use in teaching in hospitals, for research findings and reports and as protection to the physician in the event of a threat of a malpractice action (Grossman 4175). [68]

221. Medical ethics emphasize the sanctity of the patient-physician relationship and require that information divulged to a physician be kept confidential and not disclosed without the patient's authorization (Pheasant 11392–93, Gabrieli 1407–08, Grossman 4185).

222. Confidentiality is important to encourage free communications between physician and patient (Grossman 4177, 4195–96, Elmendorf 4247, 4247A–48).

223. If medical records could be disclosed, physicians might not keep complete records (Grossman 4176–77, Gabrieli 1410–11). Disclosure of such records could also adversely affect the individual patient (Pheasant 11393–95). For example, disclosure in the case of emotional problems might interfere with the patient's adjustment to society and his personal career (Gabrieli 1409–10).

B. Respondent's Acquisition of Medical Information

224. There are valid reasons for disclosure of confidential medi-

cal information, including disclosure to an insurance company in the case of an application for a policy.[72] Under such circumstances, the physician is obliged to disclose confidential medical information if authorized to do so by the patient (RX 641A-D, "Opinion and Reports of the Judicial Council" of the American Medical Association; Gabrieli 1413, Grossman 4181).

225. Respondent obtains medical information from physicians, hospitals and clinics in connection with two of its services: the Underwriting Medical History (UMH) report and certain claim reports (Trotochaud 6404-05, 6289). **[69]**

226. Respondent's UMH service was initiated in 1966, and established as a standard service in 1967 (Trotochaud 6282, 6369; RX 654, 655). Prior to 1972, respondent also had an attending physician's statement service; this service was similar to and eventually replaced by the UMH service (Trotochaud 6281-82, 6369-70).

227. In securing medical information in the case of UMH reports, respondent performs a courier service (Trotochaud 6404-05). The objective of the UMH service is to speed the flow of medical information from medical source to the insurer (Trotochaud 6282, 6367-68; Hawkins 1052-53).

228. In preparing UMH reports, the medical authorizations used by respondent are generally part of the application forms provided by the particular insurance company (Davison 2643-44, Hawkins 1050, N. Taylor 10824-25). The application forms used by insurance companies, of which the authorization is an integral part, are filed, approved and reviewed by the insurance departments of the states where they do business (Davison 2665-66, Hawkins 1076-78, N. Taylor 10825-26). The exact language of the authorizations has varied, since different companies are subject to the regulations of different states (Trotochaud 6408) and because, at least in the past, most companies themselves prepared the forms submitted for approval (Davison 2645-46). Currently, most companies use virtually identical forms (Davison 2645). Some of the authorizations furnished by customers to respondent (from insurance applications) have mentioned Retail Credit Company by name (and respondent has encouraged the use of such forms) (Trotochaud 6408-09; A. Brown 7754; Converse 4638; Guse 12070-71; Harden 1382, 1386), while others have authorized release of medical records to the "bearer"; to the named insurance company or its "representative" or "agent"; or to the named insurance company (A. Brown 7754, Davison 2643-44,

[72] Insurance companies seek medical information in determining whether to issue or rate a life or health policy and in determining what action to take when a claim is filed (Davison 2657-58; Hawkins 1018; Taylor 10831-33, 10856; Hankin 10629-30, 10637-38).

Harden 1386–87, Hawkins 1050, Trotochaud 6408). The authorizations which refer only to a named insurance company are in the minority (Trotochaud 6408). [70]

229. In connection with claim investigations, in some instances, the insurance companies obtain authorizations from the claimants and furnish them to respondent (Trotochaud 6405–06, Hankin 10649). For example, Occidental Life required a claimant to execute and submit an authorization as part of the proof of claim (Hankin 10649–50). However, in a majority of cases, the insurance company does not supply an authorization, and respondent obtains an authorization directly from the claimant. Also, certain hospitals require the signature of the doctor in addition to the signature of the claimant; in these instances, respondent cannot use the authorization furnished by the insurance company, and it obtains one signed by both the claimant and the doctor (Trotochaud 6407). Respondent, when it obtains an authorization, uses its own form, which specifically authorizes release of the information to Retail Credit Company (or, since January 1, 1976, to Equifax Inc.) (RX 633; Trotochaud 6406). The practices of insurance companies in handling claims are subject to state legislation. In California, any resident who is dissatisfied with the handling of a claim can register a complaint with the Insurance Department, which has access to the insurance company's complete file (Hankin 10633–34). In addition, in several states, insurance companies are subject to triennial examination by the insurance authorities, and this examination includes a detailed study of the company's claim operations (Hankin 10634, Davison 2667).

230. In the relevant period, field representatives were instructed not to represent themselves as employees of the insurance company (Burk 10382). In introducing themselves to medical personnel, field representatives regularly gave their names and stated they were employed by respondent (Baranek 9699, A. Brown 7749, Burk 10382, Cooke 9974–75, Guse 12052–53, Hartfield 10494, E. Jones 12927, L. Jones 10448, J. Moss 11024, Pregler 9218, Silar 4039).[73] [71]

231. In the course of securing medical information, respondent's field representatives regularly returned to the same medical source for medical records on different patients requested by different insurance companies (Burk 10383, Guse 12054, Harden 1388–89, Hartfield 10495). In addition, several field representatives testified that, on one occasion, they would present to a single doctor or

[73] The witnesses who testified on this point stated that they had never represented themselves to a medical source as an employee of an insurance company (Burk 10382, Cooke 9975, Guse 12054, Hartfield 10495, Jenckes 82, L. Jones 10449, J. Moss 11025, Pregler 9218).

hospital, authorizations from several different insurance companies on different patients (Cooke 9975, Huntington 12602, E. Jones 12928, L. Jones 10449–50, J. Moss 11024, Pregler 9217–18).

232. Under the circumstances, it appears that those medical sources contacted for information with respect to several different patients for different insurance companies were on notice that respondent's field representatives seeking medical information were not insurance company employees.

233. The UMH report is a three-part form which has, since the inception of the service, carried respondent's name (formerly Retail Credit Company and now Equifax Inc.) in bold print at the top of each page (RX 634B–D; Trotochaud 6388–89, A. Brown 7749, Baranek 9700, Cooke 9975, Guse 12053–54, Huntington 12601, Pregler 9217). The usual procedure was to give this form to the doctor, or the member of his staff whom he had designated to fill in the information requested (Trotochaud 6290, 6452–53). One part of the form,which bears the name of Retail Credit Company, is marked "Doctor's Copy," and the procedure has been to give this copy to the doctor or other medical source for his or her records (RX 634D; Trotochaud 6386-88, 6404; A. Brown 7749–50; Baranek 9700; Cooke 9975; Huntington 12602; Pregler 9217). Consequently, the doctor and his staff could, by reading the forms which they filled in and retained, determine that the information was supplied to respondent and not to an employee of the insurance company.

234. In obtaining medical information for a claim report, the preferred method was for the field representative to interview the physician. The field representative recorded the information on a company form, which had the name "Retail Credit Company." This form was then given to the doctor for his review and signature (Burk 10383–84, Trotochaud 6290). The physician could, by reading the form, determine that the information was being furnished to respondent. [72]

235. The record will not sustain a finding that respondent's employees represented themselves as insurance company employees when they sought medical information from medical sources such as physicians or hospitals (Findings 225-34).[74]

C. Retention and Use of Medical Information by Respondent

236. The filing procedures for UMH reports and the rules as to

[74] Two of respondent's field representatives testified they stated that they represented a particular insurance company but did not affirmatively claim to be employees of such companies (Jenckes 82, Harden 1383). The testimony of these two witnesses is outweighed by the other evidence showing no deception on this point.

what use could be made of file copies, changed during the relevant period.

237. When the UMH service was first instituted, respondent retained copies of the UMH reports in the regular reference alphabetical files along with claims and underwriting reports. The file copy was stamped "PRIVILEGED FILE Do Not Use or Quote. See Mgr. or Claim Dir." (RX 654, 655; Trotochaud 6369, 6382, 6402; A. Brown 7755; Coleman 7917–18; Jenkins 5797–98). Field representatives were not permitted to quote verbatim from a UMH report in a subsequent underwriting report (Trotochaud 6381). A field representative could read the UMH report and use the information therein as a "tip" in preparing underwriting reports (Trotochaud 6382–83).[75] It was also permissible to supply a new requester with the date and name of the recipient of a prior UMH report. In April 1972, the procedure was changed to permit giving only the date (and not the name or account number of the prior recipient) (RX 656A–B; Trotochaud 6372–73, 6381). [73]

238. This procedure was changed by a memorandum dated July 11, 1972 (RX 636A–C), effective immediately, which gave instructions to "discontinue copying, quoting from, or using in any way in subsequent reports, information from UMH reference files." (RX 636A). Each branch office was supplied with a form which had to be returned to the Home Office, stating that the memorandum was received and the date on which it was received (RX 636C; Trotochaud 6384–85). Under the new procedures, the file copies were placed in a separate file drawer, filed chronologically by customer mailing date, and kept for 90 days (RX 636A–C; Trotochaud 6379–80). In addition, existing UMH reports in the reference files were purged when they were discovered in the preparation of new reports or in the course of the experting and destroying procedure (Trotochaud 6480). The change was instituted because the Company had not always been successful in assuring outsiders that UMH reports would not be used in subsequent reports (Trotochaud 6378–79). The file copy was retained for 90 days in order to take care of situations where the original report was lost (either in the mail or by the customer) and of any question by the customer as to billing (Trotochaud 6379). The field representative no longer had access to completed UMH reports because a file clerk could find a report on a given consumer in the chronological file only by thumbing through the entire file; no index of the file was maintained (Trotochaud 6380, 6383).

239. This procedure was changed by a memorandum dated

[75] Using information from a report as a tip meant "the information could not be used directly from the report, but could be used in the process of conducting the current inspectional investigation." (Trotochaud 6382).

November 26, 1973, which provided that no file copy of a UMH report was to be retained (RX 635A–B; Trotochaud 6385–86). The UMH form was revised by adding a "control" sheet (RX 634A), which contained the name of the subject of the report, the name of the customer, the medical source contacted, whether a fee was paid, and when the handling was begun and concluded; it contained no medical information (RX 634A; Trotochaud 6385–86). This control sheet was then retained in the file; the copy of the report previously designated "file copy" was redesignated "review copy" (RX 634C; Trotochaud 6386, 6400) and was to be destroyed as soon as the supervisor had reviewed it and assured himself that the report had been completed in accordance with Company instructions [74](RX 634C; Trotochaud 6386). At the same time, the procedure of leaving a copy of the report with the physician was made mandatory (Trotochaud 6388). In making this change, the Company recognized that there would be instances in which a report would be lost in the mail and that in those cases, the respondent would have to bear the cost of rehandling (Trotochaud 6387). Respondent made the change because the 90-day retention procedure led some people to think that information in the report could be used in subsequent reports. It wanted to demonstrate there was no way in which confidentiality could be violated because once the information was sent to the insurance company, respondent no longer had it (Trotochaud 6386–87). This revision of the filing system was implemented in the field (Jenkins 5797, 5803–04; A. Brown 7751–52, 7759; Coleman 7917; Paladino 8726–28; Zack 8253–54).

240. The filing procedures for claims reports which contain medical information and the rules as to what use could be made of such information, also changed in the relevant period.

241. Since at least 1960, any claim report containing medical information was stamped "privileged", with a legend stating that the claim director or manager should be consulted (Trotochaud 6420–21, 6437–38; A. Brown 7755; Eldred 11236–37; Jenkins 5798; Cf. RX 654). Prior to May 1974, claim reports were filed in the regular reference alphabetical files. Medical information in such reports could not be quoted verbatim in a subsequent report but could be used as a "tip" (CX 666N; Trotochaud 6314; *e.g.*, Burge 5097, Jenkins 5801–02, Lieber 9003, Hakey 1567–68, Laudumiey 1852–53). It was also permissible to state in a new report that a prior claim report had been made (including the customer and date) and giving the name of the doctor and hospital, dates of confinement and the cause (CX 666N, 667Z–29; Trotochaud 6314). [75]

242. Prior to February 21, 1974, if respondent received an inquiry

from a customer who supplied a valid authorization and there was medical information in the claim file concerning the subject of the inquiry, respondent supplied the medical information in the file to the second requester. This procedure was changed by a memorandum dated February 21, 1974, to provide thereafter that the information would be furnished in these circumstances only after receiving permission to do so from the medical source originally supplying the information (RX 639A-B; Trotochaud 6409-10). If such permission was refused, then respondent would recontact the source and obtain the information again (Trotochaud 6410). The change was made to comply with the rules, regulations and ethical procedures as to confidentiality which the medical profession was urging on the insurance industry (Trotochaud 6410-11).

243. Beginning in May 1974, new claim reports were placed in a separate file from other reports. During the separation process, which took approximately a year (RX 660A, 637A; Tr. 6598), previously prepared claim reports were pulled from the regular reference files and placed in the separate claim files (RX 580A-B, 638A-B; Meyer 6596-98, Trotochaud 6423-24). In June 1974, prior to completion of the separation, respondent's employees in the field were instructed to cease quoting insurance history to a current underwriting customer from previous claim files (RX 637A-C; Trotochaud 6426-28). Claim reports (including medical information therein) were not available to field representatives preparing underwriting reports after their segregation in the claim files (Cooke 10006-07, Baranek 9700-01).

244. On December 4, 1975, instructions were issued, effective immediately, that no medical information was to be kept in the claim files. All such information had to be set forth on separate forms (other than the claim report itself) and all copies of the medical attachment were to be destroyed as soon as the report was mailed to the customer (RX 647A; Trotochaud 6411-12). Again, each branch office was required to return to the Home Office a form stating that the memorandum had been received and the necessary action taken to implement the new procedure (RX 647B; Trotochaud 6412). [76]The purpose of the change was to offer the medical profession assurance that respondent would not use medical information other than to provide it to the customer requesting it, because there were still those who felt that respondent might use medical information for other purposes as long as it had such information in its possession (Trotochaud 6415).

245. In short, until July 1972, UMH reports were kept in the regular alphabetical files. And from July 1972 to November 1973, file

copies of UMH reports were kept for 90 days in a separate file (Findings 237–39). Respondent's separation of claim files from other reports began in May of 1974, the procedure taking about a year (Finding 243).

246. Prior to July 1972, information in UMH reports could be used as a tip (Finding 237). Before the separation of the claim and underwriting files, field representatives were permitted to use medical information contained in the claim files as a tip or lead in conducting their investigations (Finding 241). It was contrary to respondent's policy, when using prior medical information as a tip in a current investigation, to ask leading questions based thereon (*e.g.*, Lieber 9004, 9054–55). Field representatives were to ask open-ended questions. Nevertheless, violations of this policy occurred.[76]

247. Information from claim reports could be used as provided in respondent's manuals. [77]CX 666, the Field Representative Manual contains the following instructions pertaining to medical reports in claim files:

> Previous Claims Reports in our reference files are valuable assets in making a current report. Some give details of previous health conditions; some point to finances or previous automobile accidents.
>
> Physician Reports and Hospital Records are 'privileged files.' Direct quotations from privileged reference files and copies of them can be made only when you have an authorization signed by the subject *for the customer to which you are reporting.* The authorization should be retained in your reference file.
>
> If the current report is a Claim Report or an L&H Underwriting Report and you have no authorization, the reference file information may be used as a tip. Do not make verbatim quotations from the reference file in writing the report. Limited factual information may be given in a special paragraph and should be written as follows:
>
> > NOTE: On 7-1-68, we reported to the Blank Insurance Company, Lincoln, Nebraska, Claim #8956, in connection with a claim for sickness benefits. We found that the subject was confined to the Mercy Hospital from 4-2-68 to 4-13-68 and was attended by Dr. George White. Ailment was kidney trouble and an operation was necessary to remove a stone.

(CX 666N.) [78]

See also Claim Director Instructions, CX 676Z–14, and the Branch Office Manager Manual, CX 673Z–229. (The printer's dates are 3–70

[76] Although only three ex-employees testified that they asked leading questions in connection with the use of prior medical information as a tip, there was a potential for abuse in permitting such use of the information (Wines 379, Woicik 2888, Silar 4040–41). In view of the proclivity of substantial numbers of respondent's field representatives to utilize unauthorized shortcuts (Finding 405), the potential for such abuse during the relevant period when such records were available in the general files was substantial.

for CX 666, 3-71 for CX 676 and 3-69 for CX 673; RX 102N-O (printer's date 4-73)).[77]

248. Similar instructions were given in the L&H Manual for incorporating privileged medical information in case respondent had no authorization to quote it in a current underwriting report. These instructions were not limited to claim reports and would encompass all medical reports obtained by respondent (CX 667Z-29, printer's date 9-71). These instructions also permitted disclosure of diagnosis such as "kidney trouble" and of treatment such as "operation was necessary to remove a stone" (ibid). Respondent's procedures also permitted field representatives to use information from UMH reports as a tip prior to July 11, 1972 (Trotochaud 6382-83).

249. Respondent's instructions, even with the prohibition against direct quotation, permitted disclosure of confidential medical information pertaining to diagnosis from privileged medical reports in claim and UMH files without authorization therefor.[78] The permit-

[77] These instructions on this point in RX 102N-O are identical to those in CX 666N. However, as of July 1973, the instructions no longer permitted quotations from claim medical reports pertaining to diagnosis and treatment, disclosure being limited to dates of admission or treatment by physician or treating institution (Claim Director Instructions, RX 109B).

[78] Respondent requests a finding that:

. . . [T]here are certain basic facts [in medical records] which are not privileged, i.e., the dates of confinement to a hospital, the name of the hospital, dates of treatment by a physician, the name of his physician and admitting diagnosis, which may be disclosed without authorization (Trotochaud Tr. 6468; A. Brown Tr. 7908-09, 7912-13; Mr. Jerome Tr. 9657-58). [79]

This finding is not adopted since the testimony relied on pertaining to diagnosis is apparently in conflict: Ann Brown testified that hospitals would give admitting diagnosis without authorization (Tr. 7909, 7912-13).

The Trotochaud testimony seems to include diagnosis in the privileged category:

Q. Would you define what you mean by privileged medical information?

A. *'Privileged medical information' is that information that directly relates to the treatment or the nature of the illness.* It does not include dates of confinement to the hospital, name of the hospital, dates of treatment by a doctor, name of a doctor. That information is available to the general public.

I suggest that the *recent publicity given to the Hughes situation would bear that out. The hospital* disclosed the fact Hughes had been admitted to the hospital and date he was admitted but *did not disclose diagnosis or cause of death.* That is the difference between 'privileged' medical information and 'non privileged.' (Tr. 6468; emphasis supplied)

Gerald Jerome testified:

Q. What information was privileged?

A. Medical information that required authorization to obtain.

Q. *Was any information that was received from a doctor, or hospital that might not be privileged?*

A. *Only dates of admission and discharge and the name.* (Tr. 9657-58; emphasis supplied).

See also Model State Legislation prepared pursuant to the directions of the House of Delegates of the American Medical Association defining "confidential medical information" as follows:

(d) The term 'confidential medical information' means: (1) all information regarding a patient's medical history, condition, or treatment communicated by the patient or other person on the patient's behalf to the patient's physician or his agents or employees during the course of the physician-patient relationship or to a hospital or other health care facility or its agents or employees, and (2) all information developed by the patient's physician, his agents or employees, or by a hospital or other health care facility or its agents or employees relating to the diagnosis or treatment or medical evaluation of the patient.

(RX 672D-E; Pheasant 11378-79.)

ted use [80]of respondent's medical reports as tip information, if leading questions were asked in the absence of a valid authorization, would also result in unauthorized disclosure of confidential information. In addition, the permitted use as tip information in unrelated transactions without an authorization breached confidentiality even when leading questions were not asked.[79]

250. Respondent's brochure entitled, "Reporting Medical Information," urging the medical profession's cooperation in furnishing such data, represented: [81]

We handle thousands of hospital and medical records every month in a tactful, responsible, and confidential manner.

(CX 397A–C, printer's date 10–71.)[80]

The brochure was disseminated at a time when respondent's procedures permitted using privileged medical information in its files as tip information and disclosing nature of diagnosis and treatment.

251. Respondent's brochure disseminated to the Medical Profession, CX 397 (October 1971), represents that such reports will be kept confidential. This implies no subsequent unauthorized use will be made thereof in unrelated transactions. Such representations conflicted with instructions as to respondent's employees that such information could be used as tips in preparing other reports and that the diagnosis therefrom could be disclosed in connection with other reports even though there was no authorization for such use (*e.g.*, CX 666N). The failure to disclose such procedures to medical sources constituted the failure to disclose a material fact and was misleading.

252. In view of the sensitive nature of the information contained in medical records and the possible adverse effects on patients from disclosure of such information, the patients' consent to the release of such information should be informed (Findings 218–23; see also CX 1481A; Elmendorf 4250[81]). [82]

253. In view of the sensitive nature of the information and the

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[79] It is self-evident that use of tip information necessarily influences an investigation irrespective of whether leading questions are asked.

[80] This brochure, which pertains to reporting medical information for insurance purposes, encompasses respondent's medical reports in general.

[81] CX 1481A states:

The consent of the patient to release information should be informed; that is, the authorization form should state unequivocally by whom the information might be used, including the requesting company, its representative, or other organization related to that requesting company.

(These and other related principles contained in CX 1481A–B were adopted by the California Medical Association, Tr. 4245–46, 4254).

consequences of its release, the fact that such information would be secured by a third party consumer reporting agency which kept copies thereof, was a material fact which should have been disclosed to the consumers signing such authorizations.[82]

254. Authorizations secured by insurance companies and utilized by respondent have used language such as the following:

> To the extent permitted by law, I expressly waive on behalf of myself and each family member proposed for insurance under this application all provisions of law prohibiting any physician, hospital official or employee, or any other person who has attended or examined me or them, or who has been consulted by me or them from disclosing any knowledge or information thereby acquired and from testifying with reference thereto, and I expressly authorize such person to make such disclosures.

(RX 666, see also 667, 668.)[83]

255. The language in such authorizations would not put the consumer on notice that disclosure would be made to a third party consumer reporting agency which, for a portion of the relevant period, kept copies of such reports in its files and which could use such data in connection with unrelated transactions for which no [83]authorization had been given. Consumers signing such authorizations did not give informed consent to the disclosure of such information to respondent.[84] Respondent should have been aware of that fact, and its use of such forms was an unfair practice within the scope of Section 5 of the Federal Trade Commission Act.

256. The extensive changes in respondent's procedures which ultimately eliminated the retention of medical reports, has effectively prevented further unauthorized use of medical information.[85]

257. In any event, respondent, when it secures medical information for insurance companies, either in the form of UMH reports or in the course of a claim investigation, is engaged in the business of insurance. Respondent's acts and practices in obtaining medical information for insurance companies are, therefore, exempt from Federal Trade Commission regulation to the extent that they are regulated by state law. [84]

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[82] Essentially, there is no consumer testimony on this point. The finding that this is a material fact is based on Finding 252.

[83] The foregoing authorizations were in use by the Occidental Life Insurance Company and were furnished to respondent (Taylor 10855–57).

[84] The finding that consumers signing certain authorizations did not give informed consent when the authorization did not name the reporting agency is based on the confidential nature of the subject information and on a review of the language in the authorization. This compels the inference that the consent given was confined to the transaction for which the authorization was given.

[85] Respondent instituted procedures to eliminate retention of UMH reports in November 1973, and to eliminate retention of claim medical reports in December 1975 (Findings 239, 244).

XI. ALLEGATIONS THAT RESPONDENT HAS FURNISHED CONSUMER REPORTS AND INVESTIGATIVE CONSUMER REPORTS TO PERSONS WHO IT HAS NO REASON TO BELIEVE INTEND TO USE THE INFORMATION FOR ONE OF THE PERMISSIBLE PURPOSES AS DEFINED IN FCRA (PARAGRAPHS 16–17 OF THE COMPLAINT)

A. Voluntary Follow-Up Service

258. Respondent formerly furnished a voluntary follow-up service pursuant to which it transmitted to certain customers to whom a prior consumer report had been furnished, additional adverse information on the individual who was the subject of the report. Voluntary information was not furnished to any customer to whom a consumer report on the individual had not been furnished previously (Jenkins 5780–81, Jones 5184–85).

259. Field representatives were instructed:

> Voluntary Follow-Up Information is information which we voluntarily submit on a person upon whom we have previously reported. Any information known to the Field Representative personally or received from reliable sources, which has an unfavorable bearing on an individual on whom he has made any kind of a report, should be submitted; for instance: death, serious illness or disease, accident, bankruptcy proceedings, change in occupation which involves a hazard, arrest for some serious offense, suits or judgments, fire, fire or theft of car, etc.

(CX 666Z–35.)

260. The Voluntary Follow-Up Service was discontinued on April 29, 1974 (Jenkins 5781–82). [85]

261. Voluntary information generally consisted of public information found in newspapers or public records (Ivey 2005–06; R. Jones 5236; Jenkins 5780–81; Ledum 4663–64; Fuentes 2075–76, 2086; A. Pierce 2581; Hawkins 1085–86). It was not necessarily limited to public information, however, and could include "[a]ny information known to the field representative personally or received from reliable sources which has an unfavorable bearing" (CX 666Z–35; Jenkins 5855).[86]

262. No charge was imposed for the transmittal of voluntary information (Fuentes 2075, A. Pierce 2596, R. Jones 5188, Jenkins

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[86] As one of respondent's officials testified:

> Q. Might another example [of Voluntary Follow-Up] be information on which was developed through a representative or by a field representative during subsequent investigations and different reports?
>
> A. Certainly. The field representative could very well have developed the accident or sky diving or fire. It does not have to be a newspaper clipping.
>
> Q. Does that also apply to monetary savings?
>
> A. Yes.

(Jenkins 5885).

5784). Respondent expected to be rewarded by increased business as a result of the service (CX 666Z–35) and, the dissemination of such information must be deemed a promotional device.

263. Insurance companies receiving voluntary information sometimes had a policy in force in connection with the individual who was the subject of the voluntary follow-up and, at other times, did not (Davison 2642–43, Hawkins 1056–57).

B. Monetary Savings Program

264. Respondent's Monetary Savings Program was in effect during the period 1971 to present (RPF 248). [86]Under the Monetary Savings Program, respondent, in certain instances, transmitted to its sales force information about the subjects of previously prepared reports. This was done if it was discovered that an event had occurred which would cause an insurance company a loss and if such insurance company had earlier been furnished with one of respondent's reports which would have allowed it to identify such risk and rate or decline the application of the subject of the report (Jenkins 5783–84, R. Jones 5188, L. Smith 10576, Ledum 4665, A. Pierce 2583).[87]

265. Respondent's sales representatives sometimes used such monetary savings information as a promotional device to demonstrate the value of its reports (H. Smith 8434–35, 8443–44; L. Smith 10576; Fuentes 2074–75).

266. Most of the information transmitted to customers pursuant to the Monetary Savings Program was of a public nature, *e.g.*, newspaper clippings, police and court records, etc. (Fuentes 2086; R. Jones 5186, 5237; Ledum 4665; Hawkins 1086). Such information could also, however, be derived from subsequent investigations (Ledum 4665, Jenkins 5855). No charge was made for the transmittal of such information (R. Jones 5188, Jenkins 5784).

267. Monetary savings information could be transmitted to an insurance company which had no policy in effect on the individual involved. It could have rejected the application on the basis of the original report previously submitted (Jenkins 5856, L. Smith 10588–89). [87]

268. Respondent knew or should have known that information furnished under the Voluntary Follow-Up Service and Monetary Savings Program was sometimes furnished to insurance companies who had no insurance policy on the individual involved or who were

[87] The Voluntary Follow-Up Service differed from the Monetary Savings Program in that the initial report preceding the voluntary follow-up did not identify a risk or a hazard.

not at that time considering an insurance application on that individual (Findings 263, 267).

269. Respondent, under both the Voluntary Follow-Up Service and the Monetary Savings Program furnished information about consumers to insurance carriers when there was no request for such information and, in some instances, to customers who had no need for the information as defined by FCRA.

270. Respondent, under its Voluntary Follow-Up Service and Monetary Savings Program, furnished consumer and consumer investigative reports to persons who it had no reason to believe intended to use the information for one of the permissible purposes set out in Section 604 of FCRA (Findings 268–69).

XII. ALLEGATIONS THAT RESPONDENT HAS INCLUDED IN ITS CONSUMER REPORTS OBSOLETE INFORMATION IN VIOLATION OF SECTION 605, FCRA (PARAGRAPHS 18–19 OF THE COMPLAINT)

A. Employment Records

271. When respondent is requested to prepare employment reports covering employment experience for more than seven years and when respondent obtains adverse information more than seven years old from a former employer, as a matter of established procedure or usual and customary practice, respondent states in the reports "In compliance with the FCRA, no additional information can be reported from this former employer covering employment experience prior to seven years ago" or otherwise indicates that the Fair Credit Reporting Act does not permit the reporting of such information.
(CX 1445D, ¶ 23; CX 675U.) [88]

272. Such stock sentences were to be used only in connection with employment records (CX 675U). The stock sentence that FCRA does not permit the furnishing of information covering employment experience prior to 7 years ago was utilized only in the case of those reports where adverse information had been uncovered (CX 1445D, 675U). The limiting of the use of this stock sentence to those situations where adverse information had been uncovered indicates that its use was intended as a signal to disclose the existence of such information.[88]

[88] There are a number of ways respondent could have apprised customers of the limitations imposed on its services by FCRA without signaling the existence of adverse information in particular cases. One method might have been simply to routinely provide all users of its employment reports with a brochure setting forth the relevant text of Section 605. Such a brochure could have been enclosed with *all* reports or it could have been sent to users of the reports on a one-time basis.

273. The practice violated Section 605 of FCRA.

B. Motor Vehicle Reports

274. Respondent sometimes furnished photocopies of state motor vehicle reports with portions of the report masked out (Answer, Par. 18). Such reports dealing with individual consumers were purchased from state motor vehicle departments for transmission to respondent's insurance company customers (Hewey 6514).

275. Prior to April 25, 1971, 21 state motor vehicle departments provided motor vehicle records containing information more than seven years old. Some states provided such information as a matter of procedure; in other states, the systems to prevent the reporting of such information were not always effective (Hewey 6514–15). [89]

276. Respondent was aware that such practices by certain state motor vehicle departments made it difficult to comply with the provisions of Section 605 of the FCRA (Burge 4993–94, 4996).

277. Respondent, for a period of time after FCRA became effective, was uncertain whether motor vehicle records were subject to Section 605 (Hewey 6516). It was not until 1973 that the Federal Trade Commission interpreted FCRA to apply to state agencies which issued motor vehicle records (Hewey 6532).

278. Respondent's officials contacted state motor vehicle departments to encourage them to change their systems so that respondent would not be provided with old information (Hewey 6517). Respondent's attempts to have the states change their procedures were not always successful (Hewey 6518). Respondent persisted in its attempts to secure such changes (Hewey 6521–22). Currently, no state reports information over 7 years old in motor vehicle reports (Hewey 6529).

279. Respondent's masking out of obsolete information on state motor vehicle reports was a reasonable response to the situation facing it in the case of those states reporting such information. The record discloses no intent to signal the existence of such information in violation of Section 605, FCRA.[89] [90]

XIII. ALLEGATIONS THAT RESPONDENT DOES NOT FOLLOW REASONABLE PROCEDURES TO ASSURE MAXIMUM POSSIBLE ACCURACY OF THE INFORMATION CONCERNING THE SUBJECTS OF ITS REPORTS (PARAGRAPHS 20–21 OF THE COMPLAINT)

A. Pressure To Produce Protective and Declinable Information and Respondent's System of Quality Audits

[89] Alternatives to the procedure actually followed, such as retyping the information on a non-official form would have made it obvious that the original record had been altered (Hewey 6521).

(1) Protective and Declinable Information

280. Respondent's Branch Manager's Manual states:

Actionable Information: This is the basis on which we sell our services. The terms "Protective/Declinable" and "Actionable Information" have become descriptive of the information we develop for our customers and the terms are used interchangeably. Insurance companies must have information to properly rate each acceptable risk, as well as to decline or cancel the "poor risk."

(RX 107Z–153; CX 673Z–166.)

281. Declinable information is adverse information on the subject of a report which might cause the company to which he is applying for an insurance policy to refuse to write such a policy (Bresnahan 583).

282. Protective information is information which is not sufficiently serious to make the case declinable but which may have an effect on the way the insurer rates it (Bresnahan 583).[90] [91]

283. Significant information is used in connection with claim reports to refer to information that would be helpful to respondent's customers in evaluating claims (Monarch 8565, 8573). Protective and significant information are considered synonymous (Stubbs 9279).

284. Selective information is a term used by respondent in connection with its employment reports. It refers to particular qualities or skills which would make a person a desirable prospect for employment (Jenkins 5790, 5858–59; Hale 12681–82, 12730; Bresnahan 692–93).

285. Respondent's normal procedure is that adverse information must be confirmed by at least two sources (Jenkins 5789). An exception to the rule occurs when only one person, because of his peculiar relationship to the subject, has access to the information.[91] In that case, it is reported with an indication that it came only from the one source. Normally, protective and declinable information from one outside source, which cannot be confirmed, is not reported (*e.g.,* Baranek 9713–14, 9725–26; Garcia 13131; Fuentes 2030; Johnstun 12320). Such information, although derived from a source other than an employer, may be reported, however, with a confirmation note stating that the information was obtained from only one source and the reasons why it could not be confirmed (Horner 9893; Todd 9769–70, 9788–89; Lowitz 8791–92; Tilden 11817).

286. The general rule, as stated in respondent's Field Representative's Manual (March 1970), is that unfavorable information received

[90] The terms "protective" and "declinable" are no longer used by respondent. A current term used by respondent is "features" which combines the concepts of protective and declinable (Lieber 9106).

[91] An example of this would be an employer (Vogen 12206).

from the applicant or insured should be confirmed just as carefully as though received from outside sources (CX 666Z–2 and 3). If the information is personal, covering health, habits or personal reputation and cannot be confirmed, then the field representative is to make a put-up to his supervisor (ibid; see also RX 102Z–3). In practice, adverse information coming from the applicant himself is to be confirmed if possible. If it cannot be [92]confirmed, it is to be attributed to the applicant, noting that it could not be confirmed elsewhere (Jenkins 5789).[92]

287. Public record information does not need to be confirmed by a second source (Maust 8278, Vogen 12205).

288. The confirmation of protective and declinable information may require the field representative to contact one or more sources over and above the number otherwise required for the particular report (Garcia 13130–31, Getz 12388, Vogen 12205–06).

289. Respondent's determination of whether a case is protective or declinable is based on its estimate of the action that a majority of its customers would take. Respondent recognizes that not all companies take the same action on the basis of the same information (CX 1029A).

290. Respondent kept records of field representative and branch office performance in the development of protective and declinable information. The purpose was to monitor performance by respondent and to determine the value of its service to customers (Jenkins 5790).

291. Respondent's field representatives, as a matter of established procedure or usual and customary practice, recorded daily on standardized forms (Form 930) whether each completed report contained information which the field representative believed to be "declinable" or which he believed contained a "protective feature" (CX 1445D; RX 107Z–155).[93] [93]

292. Respondent's branch office managers were instructed that:

> . . .[t]he 930 should be reviewed regularly throughout the month to insure that all Field Representatives are developing a reasonable percentage of actionable information. Local management can judge from his territory and the types of cases he handles in what range this should fall. . .

(Branch Manager's Manual, CX 673Z–169.)

293. Branch office officials maintained on respondent's Form 105–A, total figures derived from the field representative's Form 930s, showing the percentage per month of protective/declinable

[92] However, many witnesses testified that if the adverse information is secured from the applicant, there is no need to seek additional confirmation (*e.g.*, Brown 7007–08, Hilderbrand 12009, Vogen 12205).

[93] This practice was discontinued January 1, 1976 (Browning 6065–66).

information he developed, as well as information concerning his production (Curtis 7148–51).

(2) Utilization of Quality Analyses or Audits

294. The audit division of the home office Research Department, in the relevant period, conducted quality analyses audits. Generally and traditionally, respondent conducted audits by branch offices and grouped those offices for regional results (Browning 6054).[94]

295. Such audits measured on a statistical basis, branch office performance with respect to the production of protective and declinable information and the branch office's performance with respect to "below standard underwriting" and "below standard operating"[95] (Browning 6053, Jenkins 5791, Sandor 6912–13). [94]

296. Respondent kept historical records based on the quality audits of percentages of protective and declinable information obtained by the Company as a whole, by regions and by branch offices (Jenkins 5790, Fausold 10224–25, Eldred 11247–48). The corporate averages were based on analyses of thousands of reports (Loar 12835–36, Eldred 11247–48, Golderer 8646) and changed yearly (Loar 12857; Bresnahan 715; Fausold 10229, 10244–45).

297. In 1975, respondent changed the audit procedure so as to get regional rather than individual branch office results (Sandor 6915, 6938). Effective January 1, 1976, it ceased auditing protective and declinable information, as well as the below standard operating and underwriting items (Sandor 6920, 6928; Brown 6975–76, 7002). Currently, the audits cover source selection and completeness, as well as report wording and clarity of presentation (Browning 6052-53; J. Brown 6975–76, 7002).

298. In the life and health line, a branch office was the subject of one or two quality audits a year in the period 1971 to 1974 (Sandor 6912, Hermo 8586). Also, a quality audit of a branch office's automobile reports was conducted once or twice a year in that period (Yox 8537).

299. Respondent's officials were concerned with performance on the below standard operating and underwriting categories as measured in the audits (*e.g.*, see CX 1229A–B, 1269A, 1127A). However,

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[94] Branch offices might also conduct report audits independently at the local level (Jenkins 5819).

[95] "Below standard operating" refers to deficiency in clerical detail (*e.g.*, typographical errors) in the report, while "below standard underwriting" refers to deficiencies in content such as failing to ask certain questions (Browning 6053; Sandor 6913, 6916).

"quality" to respondent's employees in this context, referred primarily to protective/declinable information (Hakey 1724–25).[96] As stated by the Regional Vice President for the New York Metropolitan Region in a memorandum to his managers on May 8, 1974: [95]

Notice the big questionmark where it counts the most. In Protective and Decline we didn't have a single office listed, and that's god awful to say the least.

(CX 1290A–B.)

300. The Seattle branch manager who, in a regional Automobile Quality Analysis, came up with 78 percent of its reports containing protective information and 9.1 percent containing declinable information was congratulated on his performance in "this all-important area" (CX 1229A).

301. The only measure of usable information in the home office audits in the period 1971 to 1974 was the recorded percentages of protective/declinable information (Curtis 7334-35, Moore 10094).[97]

302. The branch office received no notice of an audit, and the cases to be sampled were selected by the Research Division (Sandor 6912, Jenkins 5791).

303. Once the package of cases was received from the branch office, each case was reviewed by an analyst measuring usable or protective and declinable information and the below standard operating and underwriting features (Sandor 6913). Certain audits measured only the protective/declinable information feature (CX 1123A; Sandor 6927–28).[98]

304. After completion of the analysis, the results were tabulated and summarized on a cover sheet showing the number of cases sampled, the dates the audit was taken and the percentages of the items measured. The entire package was then turned over to the home office Operating Department for handling in the field (Sandor 6916, 6918). The audit results were transmitted to the Regional Vice Presidents by the Operating Department with such comments as it deemed appropriate. The Regional Vice Presidents then took up the audits with their respective branch offices (Jenkins 5791). [96]

305. Branch office performance was measured against historically determined levels. The branch offices were ranked for the performance category tested, in upper, middle, or lower thirds. The ranking was determined by relating current performance of a

[96] One field representative was informed by his assistant manager on April 17, 1973, "You know that the words quality and decline are now synonymous and we are being paid for developing actionable information . . . " (CX 982B).

[97] Employment reports were an exception (Finding 284).

[98] This procedure has been discontinued (Sandor 6928).

particular branch office to the performance of all branch offices in the preceding year (RX 710).

306. The following figures from CX 1254B, a Life and Health Report Quality Analysis for the Tulsa branch office in the Southwest Region, are typical of the statistics detailed in a home office quality analysis or audit in the relevant period:

	Current Analysis		*1972 Combined Results*	
	Prot./Dec.	*Completed*	*B.O.*	*Org.*
Number of Reports		70	–	52,970
Total Protective		15.7	20.0	19.0
Major Features:				
Habits		0.0	.5	1.0
Reputation		1.4	2.0	2.3
Reckless Driving		1.4	2.0	9
Declinable		1.4	3.4	4.5
% of Protective Reports Having:				
Over 20 points		0.0	2.4	1.3
11–20 points		0.0	4.9	9.1
8–10 points		18.2	22.0	16.9
5–7 points		27.3	24.4	21.6
Under 5 points		54.5	46.3	51.1
Below Stand. Underw		32.8	21.2	19.2
Below Stand. Oper.		18.6	21.2	16.3
# Pts. Graded BSU & BSO		36	–	–

[97]307. In this instance, the Tulsa office was in the lower third for all categories, viz., protective and declinable information and below standard operating and below standard underwriting (CX 1254B). The foregoing figures show that, in this audit, 70 reports were analyzed; that 15.7 percent of the Tulsa office reports had some protective information and 1.4 percent, declinable information. The respective percentages for below standard underwriting and below standard operating were 32.8 and 18.6 percent (CX 1254B; Loar 12853). The corresponding figures under the heading 1972 Combined Results under "Combined BO" are the consolidated figures for the combined branch offices in the region for the previous year. The last column, "Result Org." sets forth the corresponding figures for the

preceding year for the entire organization (Loar 12853–54, 12856–57; CX 1254B).[99]

308. Branch office performance with respect to protective/declinable information was included in the assessment of whether an audit was satisfactory (Jenkins 5818). And, managers were concerned with passing audits and obtaining acceptable levels of protective/declinable information (Hakey 1723).

309. Respondent's employees were told in connection with their appraisals of their unit's performance on audits with respect to production of protective/declinable information, that it is the production of such data which sells the service and keeps respondent in business (CX 778A,[100] 1116B, 1187A, 1254A). [98]

310. Respondent's employees in the field were "extremely sensitive to analysis results—good or bad. They [had] a definite effect on the Manager's morale, the Manager's individual bonus, and the morale of the [Employees]" (Letter, August 27, 1973, from a Regional Vice President to a Home Office official, CX 766, 770).

311. There was considerable rivalry among respondent's offices, and everyone wanted to be at the top of the performance category in terms of all phases of branch office performance measured by quality audits, including production of declinable information (Loar 12836–37; CX 783A–F).[101] Regions also competed with each other with respect to ranking in the quality audits (CX 1070A, 1146A).

312. Performance on the quality analysis was a factor considered in the awarding of bonuses under the Management Incentive Plan. Branch managers were reminded of this by their Regional Vice Presidents, *e.g.*,:

> You, no doubt, are wondering how this fine showing will affect your management incentive measurement. It will affect it in a positive way, in most cases, in that I will add to your recorded points on quality because of automobile analysis results . . .

(Regional Vice President to Managers, Western Operating Region on June 6, 1974, CX 1146A; see also CX 1194A and 1269A).

313. Field representative performance on quality audits was one

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[99] The regional and national results in such audits reflect the averages for the year preceding that in which the audit took place (Loar 12856–57).

[100] *E.g.*, "The results can only be termed *'excellent.'* We scored in the upper third grouping in both protective and decline . . .

* * * * * * *

. . . This is what keeps us in business . . ."

(CX 778A.)

[101] Sometimes, a Regional Vice President was satisfied with performance in the middle third (*e.g.*, see CX 1309C; Hale 12673–74).

factor among several to be considered in salary recommendations by the branch manager (Eldred 11327). [99]

314. If a particular field representative consistently failed to develop protective/declinable information, he could be subjected to additional training or retraining (Jenkins 5792).

315. To obtain protective/declinable information, field representatives were instructed that they should ask the full range of questions (Baranek 9723; Cooke 9997-98; Landreth 12139, 12150-51; Saltzgaber 11971-72; Brothers 7432-34;[102] Paladino 8732-34; Zack 8230; see also CX 1229A); see logical sources (Cooke 9988, Elmendorf 11574-75, Huntington 12629-30, J. Moss 11048, Saltzgaber 11971–72, C. Smith 8374, Weston 10709); and try to obtain direct interviews with the applicant (Hakey 1715–16, Saltzgaber 11971–72, C. Smith 8374, Elmendorf 11574–75).

316. The applicant is considered one of the best sources of protective and declinable information (Miller 11715–16, Bresnahan 736, Hakey 1716, Eldred 11249). Respondent, for that reason, emphasized the importance of obtaining direct interviews with the subject of reports (C. Smith 8372, Bresnahan 718, Bigham 8600–02; see also CX 1229A).

317. Respondent's branch managers were reminded in connection with the quality audits that there were corporate objectives to be met in connection with the production of protective and declinable information:

> The attached will give you a quick picture of the Region's results, as far as this First Analysis is concerned, and you will note that we held our Protective and Declinable levels, but we are falling somewhat short of Corporate objectives. [100]
>
> Several large offices failed to show up well, and, of course, this causes the Regional statistics to suffer.

(Regional Vice President to All Offices—South Central Region on March 22, 1972, CX 1187A).[103]

318. Regional Vice Presidents urged their branch managers to secure sufficient protective and declinable information to qualify for top third ranking in the audits, and branch managers assured their superiors of the desire to achieve that goal. For example:

(a) I know you and your people are going to be disappointed with the Declinable of 5.4% in the second round analysis, especially in view of the 14.6% Declinable achieved on the first round Auto Analysis; but I also know that the personnel in

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[102] ". . . it has to be talked about to our Field Representatives to make sure that they fully understand that *all questions have to be asked in all instances* in order to extract the fullest amount of information available on any given report." (Brothers 7432, emphasis supplied).

[103] Declinable and protective results for the region in the analysis referred to were in the middle and lower third, respectively; (CX 1187B).

Albuquerque will immediately set about to make sure the next round analysis will reflect only upper third rankings in all categories!

(Regional Vice President, Dallas, to Manager of Albuquerque branch on October 30, 1973, CX 772).

(b) The complete results of the Second Round 1972 Quality Analyses are in. Our Region, at 19% Protective and 4.5% Decline, finds itself squarely in the Middle Third. This is disappointing, and I will tell you why. Our people, as a whole, in the Northern Pacific Region are too good to have a record other than in the Upper Third, and I would hope that you agree with me.

(Memorandum to Managers in Northern Pacific Region from Regional Vice President on November 13, 1972, CX 1070A). [101]

(c) As you know, the L&H Analysis was completed last Fall, and I have written most of you concerning the results.

I thought you would like to have a photocopy of the master page, showing just how the South Central stacked up.

As you can see, *some of the larger offices are in the Lower Third, and this pulls our percentages down considerably.* Also, some offices that have consistently delivered a high Declinable percentage are shown in the Middle and Lower Third, and I would expect that these offices would normally perform at a much higher level.

This is just informative—you have all received your own record, but I felt you would like to see how others performed.

I can't help but congratulate Dayton and Lexington as they are in the Top Third on both Protective and Declinable. Louisville, a large office, is quite close, and several other points could have a much higher showing with one or two more Declines.

The Automobile Analyses are starting to come in now, and I have seen two of these—both had a substantial Declinable figure (Dayton and Bowling Green), and their figures are going to be hard to beat.

Good luck to both of them, but I hope all the rest of you come up with an even higher showing. As rapidly as I receive the Auto Analyses, I will send them on to you.

(Regional Vice President to Managers, South Central Region on February 13, 1973, CX 1222A; emphasis supplied). [102]

(d) We were pleased with the improvement in the development of protective and declinable information.

* * * * * * *

Even though there is improvement in our results, we still have a way to go to

reach the upper third category which we are definitely trying to shoot for. We feel this goal is attainable and are striving hard to further improve our results.

(Manager, Miami branch to Regional Vice President, Jacksonville, Florida on June 27, 1973, CX 837).

(e) All of us naturally would like to be furnishing customers with a service that ranks above other offices and other regions. All of us would like to be in the top third as we measure an office and region.

We did reach the top third as far as protective information is concerned. We missed the top third on declinable by 0.4%, our regional performance for 1973 being 4.6%.

(Regional Vice President to Managers, Western Operating Region on September 24, 1973, CX 1127A).

319. Field representatives were advised by their superiors that they were expected to develop protective/declinable information and, on occasion, they were instructed to achieve specific percentages in these categories or that the percentages which they had achieved were too low. The following instances are illustrative: [103]

(a) Jim, I have recently completed an analysis on 55 L&H cases completed by you between the dates of 3-13-73 and 3-22-73.

Out of the 55 reports, you had six Former Resident Address Reports on which you could not obtain a direct interview. You interviewed on 27 for 55% interview. *You had seven protective for 12.7% protective. You had no declines.*

Jim, this is a very poor analysis and certainly after all of the meetings we have had and the literature that has been discussed in regards to protective and declinable and interview percentages, I would have expected this to have been much better. A reaudit will be made shortly and it will be necessary that your figures improve considerably. You should be hitting somewhere in the neighborhood of 70% interview on your L&H cases. *Your protective should be exceeding 21% and your declinable should be exceeding 5%.*

You are well aware of the fact that the Home Office will be pulling a Quality Analysis shortly and if very many of your cases get into that analysis, based on these reports that I have just reviewed of yours, you would actually pull the office down instead of helping it. I know you don't want to have that burden on your shoulders, and I intend to be working closely with you in this respect. [104]

(Manager, St. Paul, Minnesota to one of his field representatives on April 4, 1973, CX 1199;[104] see also CX 1200, a memorandum by the same author to another field representative to the same effect. Copies of these documents were sent to the Regional Vice President; emphasis supplied).

[104] The figures of 21 percent and 5 percent corresponded to the home office figures breaking down performance into upper, middle and lower thirds. The manager, in this instance, desired to achieve upper third performance (Bigham 8602).

(b) Out of 46 Automobile reports you had only 34.8% protective information. The bulk of this was on losses with driving reputation running second. This included information developed through MVR records and can almost be discounted. You only had 2 cases containing protective information concerning neighborhood and environment along with two each of physical impairments and youth or elderly risks. You had one protective on personal reputation.

Your declinable record was very good with 6.5% or 3 cases out of the total 46. These involved losses, two, and one on physical impairment.

(Manager, New Orleans office to field representative on June 21, 1972, with copy to Regional Vice President, CX 1180A).

(c) Finally during January *they were informed that until such time as each individual met the declinable objective for both the Special Narrative and Special Life areas, there would be no salary increases for any members of the unit.* As a result every single member of the unit is overdue for a salary increase by at least three months and some as long as six months. *I do not intend to recant on this area.* [105]

They have also been informed that should the results not be vastly improved by the end of the first quarter of 1971 that their first quarter bonus is in serious jeopardy and will be cut based upon their qualitative performance. You are well aware of the Frank Wibber situation, and this has had a telling effect upon the Specials Unit.

(Manager, Newark office to Regional Vice President on April 5, 1971, in connection with a special life Recheck Analysis, CX 1283A; emphasis supplied).

(d) Mr. Phillips, in the past year since I have been in Manchester has been rated a substandard investigator due to quality of his reports. Three recent report appraisals on substandard work led me to outline the terms for his continued employment to be immediate increase in quality and more decline and protective information. To accomplish this he would be transferred to the Keene Sub-office where he would come under strong supervision. Mr. Phillips decided he did not wish to change offices and therefore, resigned. In an appraisal completed two weeks after he was given notice that he must transfer there was improvement in report quality and only because of that would I consider him eligible for reemployment.

("Employee Leaving Company" form, dated September 25, 1972, concerning field representative in Claremont, New Hampshire suboffice, CX 1346A–B). [106]

(e) In the Salt Lake City office, the "manager did put out a sheet to each individual inspector at that time. If he felt you had a low percentage, he would indicate that. He would say, 'You should be paying maybe a little more special attention to your questions and getting your questions answered.' The sheets would contain notations such as 'Your decline ratio is a little low. Work a little harder and try to get it up a little more. That's about right. Good.' " (Getz 12395). Field

representatives in Salt Lake City received such sheets from the manager each month (Getz 12399–400).[105]

(f) On May 9, 1973, a San Mateo field representative was informed that one decline out of 87 cases was not acceptable "and greatly misses the company standard of 4% decline minimum" (CX 1244A; see also CX 1246A to the same effect).

(g) The manager of the San Mateo branch office expected his unit to meet the organization averages:

I think overall, we will come up with something in these organization averages that I have been furnished, like four per cent [declinable information] (Eldred 11259).

(h) A supervisor in the San Mateo branch office was put on probation when his unit's production of declinable information was considered too low. The manager taking the action stated: [107]

In connection with my specials quality survey completed in December where the unit dropped to 2% special narrative and 4% special service declinable as outlined in the report quality manual, I placed Mr. Ledum on probation for 60 days as a supervisor, this was in a memo to him on 1–11–74.
(RX 446B.)

(i) I have received replies to my correspondence of October 18 from all but three managers. From the tone of the replies, *it is obvious, and gratifying, that all managers heard from are very much aware of the need for quality reports and are already taking action with field representatives who are not developing the expected portion of declinable information.*

The replies received tell me that the managers have given this a great deal of thought and are determined to do what is necessary to assure good performance on the part of each field representative.

Being convinced that managers are already taking action where needed, *I will not at this time, make the completion of a street analysis on low performing field representatives mandatory for a salary increase.*

(Regional Vice President to Managers, Western Operating Region, November 15, 1972, CX 1265; emphasis supplied). [108]

320. A field representative in the San Mateo office set for himself (in a consultation with his branch manager) the goal of 6 to 7 percent declinable and 60 percent protective information to be achieved in 12 months (CX 1524C; Elmendorf 11583; see also CX 1504C).[106]

321. In the San Mateo and Santa Monica branch offices, supervisors kept charts concerning the production of declinable information

[105] This practice stopped in the summer of 1974 (Getz 12398).

[106] This field representative's goals were recorded on his Personnel Appraisal Report (CX 1524A-E), a form filed for field representatives which were considered candidates for developmental training or advancement into management (Tr. 11582).

by each field representative (Eldred 11244-45; Silar 3932; Milligan 4566, 4589).[107]

322. Respondent's Regional Vice Presidents and branch office managers were furnished with a document entitled "Managing Report Quality" (CX 1352A-1352Z-9; Bresnahan 658). It assigned point values for various items of protective or declinable information.[108] [109]The purpose of distributing CX 1352 was to enable local management to determine whether they had a protective or declinable case (Hakey 1638 39). If 10 points were assigned in a report on the basis of one item, the case was considered declinable; if no one item was valued at 10 points, then the combined score for various items had to exceed 10 points for the case to be rated declinable (Hakey 1641).

323. Respondent's Home Office, in reviewing cases in an audit, followed the point system contained in "Managing Report Quality" (Golderer 8689).

324. "[Managing Report Quality] is a training tool. It is an assist. It is a guide. It is an aid. It is a helper in counseling" and "[it] is an integral part of the put-up system" when the field representative tells his supervisor what he has developed (Golderer 8687). [110]

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[107] The chart in the San Mateo office was discontinued shortly after Mr. Eldred became manager of that office in early 1972 (Tr. 11245).

[108] *E.g.*, CX 1352 outlines the following point system for personal and family reputation in that section dealing with automobile reports:

FEATURES	*INSURED & OD'S— INSURED AUTO*	*OD'S— OWN AUTO*
H. REPUTATION—01		
• • •		
2. *Personal*		
a. Associates—immoral, gangs, hoodlums, etc.	10	5**
b. Immorality—present and pronounced	10	5**
c. Immorality—pres. mild or past severe criticism	5	2**
d. Domestic difficulty at present (e.g. divorce not final if car purchased prior to separation—not applicable on OD's)	3	-
e. Arrests or convictions (except Traf. Viol., see point I B 3) (Consider nature, number, recency, ct. action, etc.)		
(1) If serious and/or recent	10	5**
(2) If minor and/or in past	5	2**
f. Presently on parole		
(1) If for serious offense	10	5**
(2) If for a minor offense	5	2**
g. Dishonorable military discharge	8	3**
h. Communist	10	5**
i. Suspicious fire loss (Car or otherwise)	8	3**
3. *Family*—Member of family who does not drive generally criticized	2	-

** May be considered for maximum number of points if information applies to parents of dependent minor insured, or to spouse.

(CX 1352V-W.)

325. It was Company policy that this manual not be distributed to field representatives (CX 1352A; Hakey 1639). Nevertheless, there were instances where this policy was violated by local management, and copies of the manual were distributed or made available in whole or in part to field representatives (Hakey 1639; Eldred 11323).

326. Protective/declinable information in the form of habits, reputation, and reckless driving information was measured separately under the heading "Major Features" in quality audits and compared to regional and organization-wide statistics on these items. (*E.g.*, see CX 1254B.) And, Regional Vice Presidents brought to the attention of their branch managers, results in this area falling short of the organization averages (CX 1116A).

327. On the basis of quality audits, personnel in the branch offices were pressured to produce protective and declinable information involving habits and reputation. For example:

(a) When I review the Major Features section I'm pleased to see that you are substantially higher than the organization on habits information. Far too frequently in some of the other audits we are missing that item by a mile. Reputation and reckless driving in Hartford need increased emphasis obviously.

(Regional Vice President to Manager of Hartford office on October 8, 1973, CX 963A; see also CX 1309A, Regional Vice President to Manager, New Orleans office on April 10, 1973).

(b) It is also disturbing to me to see we had no cases with habits information. As much as we have written and talked about the Indepth Interview and the developing of habits information we still haven't gotten the message across in Miami. You certainly have your work cut out for you in instilling in the minds of the field representatives that we should develop more than 1% habits information. [111]

(Regional Vice President to Manager of Miami office on October 1, 1973, CX 844; see also CX 1298, 1306A–C, 1316).

328. The way in which a report was worded had a great deal to do with how many points it got with respect to protective or declinable information (Golderer 8689).

329. Respondent's local management, in its concern with scoring well in the home office quality audits, was concerned with persuading the field representatives to use phraseology in the reports facilitating a good score. For example:

(a) . . . We did have cases in the analysis which would have been graded decline, except for a slight change in the terminology the field representative used.

We will continue to work on terminology with our people. We are developing the information. We just seem to have difficulty getting the precise wording, which would put the decline across.

(Manager, Albuquerque branch office to Regional Vice President on February 14, 1973, CX 775).

(b) We notice a continued tendency to use the phrases, 'it is believed', or 'sources believe.' Try to eliminate this and just give the specific information without these comments, which tend to disturb the confidence of the underwriter in our report.

(Manager, Albuquerque branch office to Gallup suboffice on June 21, 1972, CX 1565A). [112]

(c) Many of these cases should very well have qualified for decline information but our investigators stopped just short of answering the final question or glossed over very detrimental information with a blanket statement stating that the man was a good driver or had no personal criticism or gave him some other good pat on the back or fine recommendation which overshadowed good decline information . . .

(Manager, Manchester branch office to Regional Vice President on May 26, 1972, CX 1340).[109]

330. Similarly, the Regional Vice President wrote the manager of the Manchester, New Hampshire branch office:

Unfortunately, Protective at 7.5 is in the lower third and this combined with your 15.1 in the first round gives you a combined of 10.00 protective all of which are in the lower third. At the time of my visit to your office we discussed quality and you had set up a definite program but obviously this hasn't got the results which are needed. One of the biggest problems was that when your people would develop declinable information it was worded in such a way that its effectiveness was decreased. These were usually such comments as; 'this is the only known instance of driving while intoxicated' or that the subject had stopped drinking completely three months ago and was now reformed. [113]

(Letter, October 13, 1972, CX 1342).[110]

331. Certain managers and Regional Vice Presidents did not believe that the audits were necessarily representative (Hale 12676;[111] see also n. 113, 114, *infra*).

332. The same audit results in terms of protective/declinable

[109] The explanation of the author of the document, that it was intended merely to ensure that logical sources be selected (Tr. 8538-41), has been considered. It does not overcome the plain meaning of the document that favorable comments overshadowing good decline information be eliminated.

[110] Subsequently, on October 16, 1972, the manager of the Manchester branch office wrote his Regional Vice President, stating in pertinent part:

We have made a number of individual report appraisals and some rehandling on the street for a number of Field Representatives since your meeting and we are taking closer put-ups on all protective cases with an eye toward declines. In addition, I am personally reviewing declines as marked on 930s and sending back coaching points where the information does not qualify.

(CX 1343B.)

[111] "As I told you earlier, I do not hold a lot of credence in the figures that come out from an audit from Atlanta, and this is one of the big reasons is because when the cases are pulled in Atlanta, it is pulled on a daily basis, and not necessarily pulled by a cross section of every individual that you have in the Branch Office, and not necessarily geographically of the territory in that Branch Office." (Tr. 12676; Regional Vice President, Gulf Region).

information could not be expected for all offices because of differing geographic as well as economic and social factors (Golderer 8668).[112]

333. The percentage of protective and declinable information which a field representative is able to develop differs by the area in which he works (Bigham 8603). [114]

334. The home office quality audit procedure, despite such differences, measured each region and each branch office against organization-wide results for the preceding year (see Finding 305).

335. Due to the sample size involved in the quality audit, it is questionable that such analysis constituted a valid survey of the performance of a branch office in the production of protective/declinable information at any one point in time (see Curtis 7279).[113]

336. Similarly, because of the sample size utilized in most audits, they did not give a representative measure of the particular items surveyed such as habits information (CX 1130A).[114] [115]

337. Despite the view that a particular audit (81 cases) represented only a minute percentage of the reports prepared by a branch office, the Regional Vice President for the Gulf Region, advised one of his managers of the branch on the basis of that audit:

> You did an outstanding job under Major Features in developing reputation—just about twice the Company average, but *you dropped the ball on Habits information. This is the area where we definitely need some additional work.*

(CX 1306A–C, memorandum dated October 3, 1973; Hale 12711–12; emphasis supplied).

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[112] Even within the confines of a particular borough of New York, there is a wide spectrum of people and information (Golderer 8668).

[113] ". . . The reason they quit [making home office quality audits] was because they felt that taking 50 reports, pulling 50 Life reports out of my office this week and then saying that is the results of your office, it is the results only for those 50 cases . . . " (Curtis 7279). Under the circumstances, "An audit was kind of like the luck of the draw. One time you might have an outstanding results, and six months later with the same people the results would be different." (ibid).

[114] As noted by one Regional Vice President:

> I still do not feel that one analysis gives a fair measurement of information being developed on one feature such as habits, when we measure only 100 to 150 reports, and when our organization average runs only one such report to every 100 cases. Habits cases are not necessarily developed on a regular schedule. An office might go a week without developing a protective habits case. If the cases for the analysis are taken during that week, then the office would show up with zero protective on habits.
>
> * * * * * * *
>
> The thought that I want to convey boils down to the fact that I do not feel that I can look at one analysis and say that an office is doing a good job or a poor job of investigating. Where I accept region results as being fairly indicative of the type of service being provided from the region, it is more difficult to accept the individual office measurement as an accurate measurement.
>
> (Regional Vice President, Western Region to Vice President Operating on September 27, 1973, CX 1130A–B).

338. On April 10, 1973, the same Regional Vice President wrote the manager of the New Orleans office as follows:

Bob, our Auto Decline since 1971 has retrogressed pretty badly. *I am sure you are going to be upset about the attached audit.*

There were 161 cases involved, and not one habits case among the whole lot. You had only 1.9% impairments, so you can see under these major features that there is a lot of work to do. **[116]**

Bob, I would like to know what you are going to do as far as Report Appraisals and Field Representative Case Handling Appraisals are concerned. *You need to develop a 'get tough' attitude with your people.*

I would not be as upset if either of the Auto audits in 1972 had been good, but the history in New Orleans for the past 1 1/2 years has not been good. As I said, I would like your specific plans for showing improvement.

(CX 1309A; emphasis supplied.)[115]

The manager in question was told he needed to develop a "get tough" attitude, although it was not possible to determine on the basis of 161 cases, what would have been satisfactory performance on habits information (Hale 12671–72).[116] **[117]**

339. Up to January 1, 1976, respondent conducted audits of claim reports, measuring performance with respect to significant information and below standard features (Trotochaud 6457–59, Stubbs 9282; CX 849A–E). Significant information, if 40 percent or less, was considered unsatisfactory in 1974 (CX 1498).[117] The level of satisfactory performance changed periodically (Stubbs 9279–80).

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[115] The manager replied:

We have embarked upon a stronger program of Quality Analysis along with Inspector Training & Performance Reviews. All of my people are acutely aware of the need to dig deeper into Automobile reports particularly in those areas involving major features of habits, reputation and impairment information.

All personnel are also fully aware of the fact that our jobs hinge on the ability to produce good quality information of benefit to Automobile insurance company's, if we are going to continue making reports of this type.

(CX 1310, memorandum dated May 22, 1973).

[116] "Q With 161 cases involved in the audit, is it possible for you to state what would have been a satisfactory performance on habits' information?

A Absolutely not."

(Tr. 12672).

[117] Protective and significant information were considered the same thing (Stubbs 9279). The Claim Audit Profile in effect in 1974 was:

SIGNIFICANT INFORMATION		*BELOW STANDARD*	
Professional:	60.0% & Above	Professional:	5.0% & Less
Superior:	50.0% to 60.0%	Superior:	10.0% to 5.0%
Good:	40.0% to 50.0%	Good:	18.0% to 10.0%
Unsatisfactory:	40.0% & Below	Unsatisfactory:	18.1% & Below

(Continued)

340. The use of audit results measuring individual branch office performance with respect to production of protective/declinable information and the ranking of individual offices results in relation to organization-wide averages had the potential for inaccurate comparisons because of the disparity of results which can be expected among offices due to differing geographic and economic factors (see Findings 332–34). The system, therefore, had the potential for generating pressure for increased production of adverse information on the basis of invalid comparisons and, therefore, was unreasonable. [118]

341. The audit results with respect to individual branch office performance on production of protective/declinable information were based on small samplings precluding assurance that the survey results were representative for the office measured (see Findings 335–36). Utilization of the system had the potential for generating pressure to increase production of protective/ declinable information on the basis of unrepresentative data and was, therefore, unreasonable.

342. The quality audit system with resultant pressure to achieve high scores in the production of protective/declinable information also had the potential for generating pressure to eliminate from reports qualifying statements, pertaining to adverse information on consumers, which could affect the manner in which such reports are construed (see Findings 329–30). The quality audit system was unreasonable on that score.

343. Respondent's system of quality audits which ranked a branch office's performance in the production of protective and declinable information against all other offices in terms of upper, middle and lower thirds computed on the basis of organization-wide figures for the preceding year impliedly set quotas for the production of such information.[118]

B. The Effect of Factors Such As Production Quotas and Time Pressures on Report Preparation

344. Salaried field representatives, by virtue of the compensation system in effect, had a quota of so many cases to produce in order to cover their salaries and expenses. The required production per field representative varied depending on his reporting standard, salary and expenses (Findings 102–29). [119]Part-time field representatives,

(Assistant Vice President-Claims to Regional Claim Supervisors on February 12, 1974, CX 1498). According to respondent's Vice President for Claims, an office would be considered substandard (Tr. 6458) if both significant information and the below standard item were below a certain level.

[118] This finding is corroborated by respondent's use of numerical ratings to define satisfactory performance under claim audits (Finding 339).

however, did not have a production standard or quota (J. Moore 8875).

345. Field representatives, on a daily basis, filled out the "Volume Control: Performance Objectives" section on the Form 930, computing their production quota and comparing actual achievement with their objective (Farra 752; CX 542).

346. Respondent's branch management was concerned with field representative losses, insisting that they be made up: *E.g.,*

> We are insisting that those field representatives who have an accumulated loss make every effort to make this loss up in October, even if it means working Saturdays. . . .

(Manager, Miami Branch office to Regional Vice President, October 16, 1973, CX 835B; see also Fuentes 2036).

347. It was the practice of the former manager of the Dearborn office when a field representative fell behind in his performance objectives for the month to "Give him a boost or a kick and possibly assign him an extra case per day or whatever it will take, whatever is necessary to bring him into the black" (Tr. 656). When his office was in financial difficulties, he wrote his Regional Vice President as follows:

> Field Rep losses continue to be an extremely costly item and all of my supervisors have been put on notice that I will not tolerate any more Field Representative losses without very good reason.

(Manager, Dearborn branch office to Regional Vice President, November 30, 1973, CX 910).[119] **[120]**

348. Time Service was another factor governing the pace at which field representatives were expected to work. Time Service was essentially the standard whereunder the branch office had a set time after receiving an inquiry or request for a report, to complete the report and mail it to the requesting customer (Hakey 1562; RX 107Z–144).

349. Time Service objectives are determined for each office; these vary from time to time and place to place. The Regional Vice President has discretion to determine the Time Service objectives for each office in his region (W. Matthews 5577). Different objectives may apply within a single office which covers both urban and rural territories. The objectives are based on historical experience and reviewed regularly (W. Matthews 5569–70, 5575; Eldred 11212–13).

350. Time Service objectives for branch office business in larger

[119] The office, at the time this memorandum was written, was "obviously under financial stress." The manager in question explained, "If you planned to meet expenses and make your monthly cost and four or five inspectors had a total loss of $800 or $1000, it would be virtually impossible to meet your cost objective in a branch office with a sizable inspector loss" (Tr. 643–44).

cities are established in terms of the Time Service index (W. Matthews 5567). For example, the objectives for the Miami branch office in 1972 were as follows: for life and health reports, an index of 1.74 with 96 percent of reports completed within 4 days and 99 percent within 6 days; for employment reports, an index of 1.74 with 96 percent of reports completed within 4 days and 1.99 with 92 percent of reports completed within 4 days and 98 percent within 8 days; for property lines, 90 percent of reports completed within 6 days and 98 percent within 10 days; and, for claim reports, an index of 2.99 and 90 percent of reports completed within 6 days (CX 506D).

351. Time Service objectives in suboffices are lower than those in branch offices because of the lower population density of territories served by such suboffices. Similarly, Time Service for work on certain circuits covering rural areas are lower than for local work (Hakey 1562–63; Jenkins 5788, 5858).

352. Branch managers were told that "fast time service can be maintained through aggressive leadership and daily inspection of the speed of the service. Time is an essential and marketable element of our business." [121](RX 107Z–144). Records were maintained to measure an office's performance in this area (ibid).[120]

353. Branch managers were held responsible for ensuring that Time Service objectives were met.[121] [122](Bresnahan 635–36). Moreover, meeting Time Service standard was one of the criteria

[120] Objectives for clearing local reports are expressed in terms of:

1. *Time Service Index (TSI):* A statistical expression of the percentage of reports cleared within an established deadline.

2. *Percentage of Cases Cleared by Deadline.*

Both measurements gauge the flow of cases through a branch office and indicate the acceptability of time service.

A standard maximum deadline has been established for each line of service—for instance, 4 days for Life and Health, 6 days for Claim. Since these are maximum deadlines, the measure of flow (Time Service Index, or 'TSI') is more vitally important because the lower the index, the faster the overall service.

TSI is computed by subtracting the accumulative percentage of cases cleared each day within the deadline period from the maximum number of days in the deadline period. For example, if 100 L&H cases are received today (the first day) and 30% are cleared today, 60% by tomorrow, 80% by the third day, and 100% by the fourth day, the TSI would be computed as follows:

4.00	
−2.70	(.30 + .60 + .80 + 1.00)
1.30	TSI

(RX 107Z–144.)

[121] There were numerous variables which affected whether Time Service objectives were achieved. Among them was the prerequisite that the office be properly organized. It was necessary to have a sufficient full and part-time investigative staff to handle fluctuations in the volume of business (Curtis 7178). In addition, an office had to have adequate supervision of the investigative staff to meet Time Service objectives. Daily controls needed to be set up to ensure that field representatives were dictating out and handling their cases on a daily basis, and the manager had to ensure that the stenographic unit was properly organized to get the dictation out on a daily basis. Measures had to be taken to ensure that reports, after they were typed, were reviewed the same day and mailed out to the customers. It was also necessary, in this connection, to provide that the reports returned to the field representatives for correction or additional work were handled the same day that they were returned (Curtis 7178–79).

considered in computation of the managerial incentive bonus (Bresnahan 575; CX 1353A–H).

354. Branch office personnel were under pressure to meet the Time Service objectives set. For example:

(a) You have a previous letter from me concerning Time Service, but just in looking at your 1205 for the month of November I hardly see why it was necessary for so many cases to get old.

Jerry, we just cannot jeopardize the service with this sizable volume of business in order to locate people.

I am expecting you to get the service in line promptly. Whatever is necessary must be done.

(Regional Vice President to Manager, Miami office, December 5, 1973, CX 832B).

(b) We are already in trouble for June as far as the movement of sub-office Life business is concerned. [123]

I am sorry to find it necessary to ask for special attention to the Life business so early in the month. .but it is *imperative* that we eliminate any over 4-day Life cases for the remainder of the month, if we are to reach our deadline objectives. Unfortunately, we have already released as many over-deadline Life inquiries as the objectives will allow for the entire month.

I know I can count on your assist. If there is anything we need to help you from here, get on the phone and call me.

(Manager, Albuquerque branch office to suboffice, June 5, 1974, CX 819).

(c) . . . I desperately need your help and assistance, most especially in the area of thoughts and ideas which will enable us to meet our time service objectives in April of 1974. . . .

. . . I can't emphasize with you enough the great importance of meeting our objectives.

(Manager, Dearborn office to Supervisors, March 26, 1974, CX 1515).

355. Field representatives were required to give explanations to management if cases become overage (Zack 8220–21). In the Salt Lake City office, a case became an expedite when it was 3 days old (Vogen 12242–43).

356. The amount of work which field representatives were expected to do on a particular case was governed, to some degree, by the price of the report. Respondent expected field representatives to not "overwork" cases. For example, if the field representative had contacted two sources in a single fee case, he should not go to a third

simply to make sure he was right. In respondent's [124]opinion, this was a question of economics in terms of the price of the report (Lieber 9110–11;[122] see also Johnson 12283–86). If a field representative had a tendency to dig too deeply, this would make meeting production requirements more difficult (ibid).

357. There are numerous variables determining how many cases a field representative could produce in a normal workday of approximately 8 hours. Illustrative of the practical problems facing field representatives are the following: [125]

> There were very many variables and you could get into situations where, let's say, you are getting detrimental information from one source, well, how long are you going to take to resolve that issue? Supposing they give you really bad information, the obligation to your company, to the consumer, to the client, if you really work at it, you might spend 45 minutes working that particular case and there goes your average right away. Or you can go into an area where you can't find a single source you talk to because they work every day and the person might be home as a babysitter or she doesn't know the people. Then that's a different case. Or you go out and you go to Northwest 17th Terrace and the case was supposed to be handléd at Northwest 17th Place because the customer made a mistake in writing up the address. Then your average goes out the window. Too many things that do not happen according to the books.
>
> . . . [I]nformation is not easy to obtain and you have to work at it. If I go meet him for the first time he may not be able to tell me the information on a given person. He will give me all the information he knows which is favorable but you first have to at least establish some sort of a rapport with me in order to confide in me especially if it is personal information and that takes time. Also, you may knock on the house and the lady will say, I'll be right with you, I'm on the phone and you've got to wait until she finishes or if she is giving the baby his milk you've got to wait or someone calls and interrupts you while you are making your interview. Those are the factors that would in this way enter into the case.

(Fuentes 2043–44). [126]

358. It was more difficult for field representatives to produce cases in some geographic areas than in others because of factors such as, the distances to be traveled in order to make the requisite investigations and the greater or lesser willingness of people to give information in different locations (Shaffer 8402, Matthews 12800–01).

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[122] THE COURT: What do you mean by overworking a case?

THE WITNESS: He has the complete information from two logical sources and he sees a third source, because he feels in his own mind, I just want to make damn sure that I have that information correctly.

THE COURT: Would this be primarily when he digs up adverse information?

THE WITNESS: A gut feeling. An indication, with two sources he carries it to a third source, or a fourth source. But, here it comes down to the scope of the investigation. A five dollar report has a certain scope of investigation as compared to a $100,000 life report which has a broader scope and it would be expected to be carried further, and the man is carrying his investigation actually beyond the scope of that particular report, beyond what could be considered reasonable effort.

THE COURT: As to the amount that is being paid for the report?

THE WITNESS: Yes.

(Tr. 9110–11).

359. The ability of field representatives to produce reports was also affected by the manner in which an office was managed. It was difficult for field representatives to do the job in an office with poor leadership (Beckett 10965). Whether a field representative could meet his production standard in a 40 to 45-hour week depended to a considerable degree on the management of the office and the production climate in that office (Lieber 9019–20, 9071–73).[123] The overall quality of the management affected the quality of reports more than any one specific thing (Brown 6977). [127]

360. In addition, the ability of individual field representatives to prepare reports varied (Lieber 9126). Experience was a factor (Pregler 9222–23).

361. In short, the field representative's ability to complete a certain number of cases in a given period of time depended on his own ability, the type of cases assigned,[124] the characteristics of the area within which he worked and the organization of his office. The need to put in overtime was a function of these variables and the flow of business.

362. Field representatives were told to record the amounts of overtime which they incurred (Lieber 9048). Respondent's field representatives, however, had little economic incentive for recording their overtime.[125] As overtime increased, the field representatives' compensation on a per-hour basis of effort decreased (see Finding 104). In addition, recording overtime increased the field representative's salary and expenses and thus, increased his required produc-

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[123] Well, the productive effort of people is dependent upon work-flow in a branch office. Work should be worked up in a manner that will permit the field rep being assigned his work early enough to meet what I consider to be an equitable balance of outside investigation work and inside office work. I look at a framework of five and a half to two and a half; five and a half out, two and a half in, or six hours out and two hours in. There has to be work available, and this entails managing the mix of business and the placing of staff. There must be a balance of organization, staff in balance with the flow of work. This must be tracked, and this is a basic function of management, tracking volume, trends by lines of service, and relating volume trends and mix in terms of dollars relating to determine productive efforts of people.

Those are the basic ingredients of adequate production in a normal day. Given those ingredients, yes. If any of these ingredients vary, then the pressure on the field rep would vary in direct proportion as to how close the office comes to this structure that I just described.

(Tr. 9020–21).

[124] See Section II, *supra*.

[125] As one branch manager explained:

Q Are some people interested in working Saturday for overtime pay?

A Heavens no, not with our company.

JUDGE VON BRAND: Why not?

THE WITNESS: Because the overtime is figured for field representative different than that overtime figure for our operating employees and inside clerical employees.

JUDGE VON BRAND: No time and a half?

THE WITNESS: That is right.

(Curtis 7271–72).

tion (Hakey 1734; Chambers 1940, 1945; Clufetos 2291; Ledum 4698; Silar 3905). [128]

363. Records of overtime in excess of 10 hours a week were questioned by management (Jenkins 5723, Fuentes 2089–90). Many field representatives chose not to record overtime because of the economic disincentives involved (*e.g.,* Ledum 4698, Chambers 1954, Monson 3252–53).

364. Respondent's overtime system is inherently, economically unattractive from the field representative's point of view (Finding 362). It is, therefore, in the salaried field representative's interest to produce within a 40-hour week enough cases to cover his salary and expenses as well as to earn a 20 percent bonus. As a result, the less time he spends per case, the greater his per-hour compensation for his efforts. Similarly, in the case of part-time field representatives as well, the less time spent on each case, the greater their per-hour compensation (Hille 4529).

365. The reporting of overtime could also affect a branch office's reporting costs adversely if a field representative had lost on his reporting standard. In short, if a field representative had trouble meeting his expenses and listed his overtime, this could increase his own difficulties and, to that extent, it could adversely affect the finances of the branch office in which he worked (Monarch 8571–72).

366. To complete their reports, field representatives were required to contact the number of sources required for the particular report and to obtain the time coverage prescribed (Section II, *supra*). Respondent has prescribed procedures to be followed if the requisite sources or time coverage cannot be obtained or if Time Service cannot be met.

367. If a report cannot be completed within the Time Service objective, the field representative is to confer with the supervisor. The case may be held over for completion, and if it is, the customer is to be sent a Form 58 notifying him that the case will be delayed (*e.g.,* Vogen 12209–10, Volrath 10991–92). [129]

368. Field representatives unable to obtain the required number of sources of information for a report after consulting with their supervisors, are permitted, under Company policy, to complete the report with less than the required number of sources. They are to state in the report the number of sources obtained and the reasons additional sources could not be obtained. The customer is asked for leads if he desires additional handling (Burge 5020–22; Browning 6064; Saltzgaber 11970, 11993; Tew 13357). In such circumstances, field representatives receive production credit for preparing reports

with less than the required number of sources (Baranek 9696, Eldred 11215–16, Zack 8260–61).

369. If a field representative is unable to obtain the time coverage for a report, he is authorized under Company procedures, after consulting with his supervisors, to write the report with the limited time coverage obtained, stating in the report, why full-time coverage was not available and asking for leads if the customer desires further handling (Baranek 9696, L. Jones 10446–47, Tew 13355–57, Chambers 1923). Under these circumstances, field representatives receive production credit for preparing reports with less than the required time coverage (Baranek 9696, Hilderbrand 12008–09).

370. Successful interviewing by field representatives was not a pro forma matter. To do the job properly, it was necessary to establish rapport with the sources contacted. As respondent's Branch Manager's Manual stated, field representatives, in interviewing during the course of an investigation, needed to be highly sensitive to the more subtle clues and remarks of the source contacted as well as "to the behavior, perceiving their implications and adapting [their] own approach and conversation accordingly. [Field representatives] must know when to talk and when to keep still, how to word [their] questions, and how to listen."[126] (RX 107Z–3). [130]

371. In addition, respondent's investigators were instructed to be objective in distinguishing facts from opinions (CX 1504G).[127] This was important in subjective areas such as habits information because "[i]n the field, it would be very difficult to get three or four people that may concur on something anyway." (Hilderbrand 12035).

372. Prerequisite to a meaningful interview was the selection of logical sources to be contacted. "A logical source is one which by reason of position or association with the subject of the report is in a logical position to give the information desired." (Field Representative Manual, RX 102W). Field representatives were admonished, "*It is how well the contact knows the subject of the report that determines the qualifications, not how well the Field Representative knows the contact.*" (ibid; emphasis in original).

373. Respondent's field representatives and branch office management were under pressure to develop protective/declinable information (Findings 317–19, 327).

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[126] Respondent's Branch Manager's Manual also stated that a sense of humor "is a powerful instrument in developing a warm, friendly relationship with sources" and "some of the most pertinent personal information is sandwiched in between homey remarks and other small talk." (RX 107Z–4).

[127] Respondent's Field Representative Manual instructs, "Rumors, gossip, and scandal must be sifted." (RX 102Z–17).

374. It was necessary, if protective/declinable information was to be developed, that the field representative ask the full range of questions[128] and see logical sources (Finding 315). An interview took longer if the full range of questions was asked (Paladino 8771). Securing adverse information could also increase the number of sources which a field representative was required to see in order to obtain the necessary confirmation (Fuentes 2043). [131]

375. All other things being equal, it took longer to develop a case with protective or declinable information than a wholly favorable report (Elmendorf 11594–95, Moss 11036, Lindgren 11454, Hilderbrand 12037, Guse 12066, Saltzgaber 11987–90).

376. In the relevant period, the telephone could be used as an adjunct to the field representative's work in the street (Brothers 7406; see also Section X). But it was the field representative's "primary function . . .to work on the street with the goal of getting face to face information from our sources" (Brothers 7406).[129] The determination of whether resort to the telephone was necessary was to be made by the manager or supervisor (Larson 12515). An attempt to clear the case on the street was to be made first (Johnstun 12286). [132]

377. Field representatives in the local unit of respondent's Boston branch office were unable to complete the number of cases per day necessary to satisfy their production requirements in compliance with Company procedures (Hakey 1597–98, 1604, 1741).[130] It was not

[128] To assist the field representative in asking the full range of questions, he was given a note form for each report which contained the questions to be asked for that particular type of report. The note form had blanks for recording the information obtained to be transcribed later. The note form functioned as a reminder or checklist to assure that the field representative did not miss any pertinent questions (Jenkins 5757–58, Brothers 7402–03, Curtis 7127–28, Bender 7665–66).

[129] See also Larson 12515: "The use of the telephone [in preparing regular life or automobile reports] at that time was not an accepted part of our procedure or normal activity of handling reports. But we did at times use the telephone when we found it necessary in order to contact the individual involved."

A memorandum in the relevant period also indicated that telephone use was to be limited:

> In connection with the other cases, Roy, the scope calls for personal interview of a minimum of two sources. As you know, this can be interview on an outside source, two outside sources, etc. The fact that we personally saw only one outside source and then used the telephone reduces the scope. It also does not fill our customer commitment. I was frankly a little surprised at Mr. Bigham's comment that if the telephone sources had not been identified by the "T" that no one would have known. Page 47 of the Inspector Manual instructs that sources be so identified. Further, all of our Marketing studies develop that Habits, Reputation, Hazardous Sports, and Drugs are the usable information features for Life customers. While telephone interviewing can produce Health Information and firm up Identity features, you may agree that in the long run it doesn't do much to secure additional information in those areas most used by customers.

(Assistant Vice President-Operating to Regional Vice President-Operating, July 25, 1973, CX 1217A).

[130] Mr. Hakey stated, on the basis of his computation, "[t]o break even, an individual would have to do a minimum of 18 reports per day to make full bonus, between 20 and a half and 21 reports a day" (Hakey 1598). Respondent introduced a computation (RX 484Z–18) showing that 14.6 cases a day were needed to meet the production standard; 15.7 cases to make a bonus of 10 percent and 16.9 cases to make full bonus. Respondent contends Mr. Hakey erred in overstating the applicable salary as well as mileage and steno expenses. The Boston branch manager's estimate for the period 1968–1974 falls somewhere between Mr. Hakey's and respondent's computations. He estimated the average field representative "would probably handle about 16 reports a day

(Continued)

possible to see two logical sources on every report, although field representatives might contact many others (Hakey 1604–05). The biggest problem in this unit was taking the time to ask a full range of questions (Hakey 1717). [133]

378. A field representative in the Claremont, New Hampshire suboffice who desired to achieve full bonus "which you needed . . . to survive" produced 23 to 24 cases a day (Crepeau 1754). He varied from Company procedures by using principally central sources and rarely filling out the note form (Tr. 1760). He needed 20 single fee equivalents a day to meet his production standard (Tr. 1778).

379. A field representative in the Baltimore branch office felt it was impossible to do the job as he was required to do it (Wines 388–89). He faked outside sources in the reports he prepared (Tr. 455, 458, 460–61).[131] And, had his cases been rechecked, he would have been fired, because there were many such instances (Tr. 455).[132]

380. A field representative in the Marietta, Georgia suboffice was assigned 18 to 22 reports a day in order to meet his production requirements (Chambers 1929–30). He normally prepared 19 to 20 reports a day (Tr. 1939). This individual was unable to prepare such reports in accordance with Company instructions in an 8-hour day (Tr. 1938–39). In order to prepare his reports, he had to work a 50 to 55-hour week, but he did not report the overtime because his production quota would have been increased (Tr. 1940). [134]

381. A field representative in the Columbus office in the period mid-April to mid-August 1972, whose goal was 18 to 20 cases a day,

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average, sometimes 17" (Tr. 8235). Even accepting respondent's calculations, the difference is not so great so as to vitiate Mr. Hakey's testimony based on his experience as a firstline supervisor. Moreover, his testimony regarding the difficulties in producing reports was not confined precisely to the 18 to 21 figure. He stated:

> It would be physically impossible for an individual to take out 18 reports or 21 reports *or anywhere in that vicinity*, leave the office between 12 and 1 o'clock in the afternoon and see a minimum of 36 people and drive from one location to another, confirm unfavorable information and see good close logical sources for the prescribed period of time. It is physically impossible.

(Tr. 1604; emphasis supplied).

In weighing computations such as RX 484 against the testimony of the witnesses, it should be further noted that such calculations utilizing devices such as applying national inquiry values to particular offices are approximations. (See Case 5922, 5888–89).

[131] In a nice area, if the property was well kept, this field representative would simply assume the good reputation of the subject (Tr. 388–89).

[132] There is disparity between the witness' estimate that he prepared 15 to 17 single fee property reports a day in 1972 (Tr 382, 421) and respondent's calculations in RX 483. According to this computation, he averaged 13.7 reports a day in the period with monthly averages ranging from 12.2 to 15.3 reports a day, and he needed an average of 12.6 reports a day to meet his production requirements, the monthly averages ranging from 9.7 to 13.7 reports a day (RX 483V–Z–2). The differences between the witness' testimony and respondent's computations are not so great that his testimony needs to be disregarded for that reason. There is no dispute that this field representative faked sources (Tr. 458). In this connection, the record also shows that his superiors for some time had been on notice that he had been "consistently sporadic in his work habits" (RX 483A). Management knew or should have known that he needed close supervision.

was unable to complete his assignments in accordance with Company instructions (Pollard 310, 316, 349).[133] He falsified sources consistently in order to facilitate production; such faking may have been on the order of one out of 15 cases (Pollard 316–17, 355–56). He faked sources in clean, *i.e.,* favorable cases and never faked derogatory information. He also falsified time coverage[134] (Tr. 318, 320). He used the telephone to conduct interviews, although use of the telephone was discouraged (Tr. 317, 388).[135]

382. A field representative in the Dearborn office in the period January 1971 to April 1971, was unable to prepare the cases assigned to her in accordance with Company procedures (Woicik 2868–69).[136] She listed outside sources not seen on reports 40 percent of the time in those instances where she was able to obtain a direct interview with the insured (Woicik 2870). [135]Field representatives in the Dearborn office were warned about excessive telephone use. "They would tell us to stop using it as much as we were." This field representative did not stop using the phone as a result of such warnings, and nothing further was done (Woicik 2872–73).[137]

383. Another field representative in Dearborn was assigned 16 to 18 cases a day and had trouble completing them (Wallace 2993–94). She was unable to prepare her reports in accordance with Company procedures (Tr. 3002). She varied from Company procedures in the use made of the telephone (Tr. 3002–03). On a relief trip to Lansing, Michigan,[138] she completed cases using unqualified sources (Tr. 3013–14).[139] And, in the case of one report on that trip, she listed a source not contacted (Tr. 3009–14, 3040).[140] [136]

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[133] He was given 12 to 13 cases a day toward the end of his employment and with carried-over cases, his assignment was 18 cases (Tr. 350).

[134] "Well, you would just go ahead and put a number in there. You know, one, or two or three years, enough that it would be credible" (Tr. 318).

[135] RX 489, one of respondent's computations which calculates that toward the end of his employment, he needed 12.9 cases a day (RX 489I) does not rebut the testimony of the witness that his goal was 18 to 20 cases a day. Respondent's calculation of the actual number of cases done by Mr. Pollard as of August 1972, 11.9 cases a day, moreover, is not inconsistent with his testimony that he was given 12 to 13 cases a day toward the end of his employment.

[136] This field representative became a part-time employee on April 1, 1971 (Tr. 2842). Her testimony for the period January-March 1971, was permitted because of the proximity to the effective date of FCRA (Tr. 2844-45).

[137] This field representative testified that, on an average, she prepared 18 cases a day (Tr. 2848–49). She may have been in error as to how many cases she needed to break even—20 to 25 cases—and she may have overestimated the number of cases she actually prepared. (Compare Ross testimony that 14 to 17 reports would have been sufficient for 10 percent bonus and 18 would have given her full bonus (Tr. 9337, 9400, 9365–66)). However, her testimony that she listed sources not seen on the reports she did do is accepted.

[138] The relief trip lasted 2 days. On the first day, she received 25 to 30 reports (Tr. 3010). And, on the second day, she received 38–40 cases (Tr. 3013).

[139] "Well, we took them [the cases] back to Dearborn with us and they were all dictated the following Monday and I used the telephone . . . Except for that one isolated incident where I couldn't get anybody I talked to at least one person and *maybe that person wouldn't give me any information but I at least talked to him so I wrote a report,* but I wrote a favorable report." (Tr. 3013–14; emphasis supplied).

[140] Q. Would you write the report from the Polk Directory?

A. On cases where I wasn't able to talk to anybody, I would write it from the Polk Directory and I'd put down my source "Mr. Polk" (Tr. 3011).

384. A part-time field representative in the Dearborn office, in order to meet Time Service requirements, listed the minimum number of sources required by a report even if such sources had not been seen, in approximately 30 percent of her cases (Hille 4514–16).[141] This field representative also wrote pat, favorable reports on the basis of sources who knew nothing about the applicant (Hille 4534–35).[142] Approximately 50 percent of her interviews of sources were over the telephone (Hille 4512).

385. A field representative in the Detroit office had to complete 15 to 16 cases a day to break even when she was making a salary of $605 a month (Dodson 3043–44, 3077–78).[143] She was assigned 18 to 19 cases a day and prepared, on the average, 15 cases a day (Tr. 3048).[144] The maximum number of cases prepared by this field representative was 20, produced when she was under pressure for Time Service or to make up losses (Dodson 3050–3056).[145] In her view, she could only do 10 [137]cases in an 8-hour day in accordance with Company procedures (Tr. 3070–71). She did not interview all the sources listed about 75 percent of the time (Tr. 3063) and she conducted 50 percent of her interviews on the phone (Tr. 3062). Sometimes, she would not note telephone use on the file copy "because you didn't want the boss to know how often you were forced to close the report on the phone" (Tr. 3063).

386. A field representative in the Salt Lake City, Utah office, who had to average 17 cases a day to meet salary and expenses, was usually assigned 20 cases (Monson 3240). The volume of this branch office fluctuated, and the lowest number of cases he took out was 12 (Monson 3243). He worked about 9 hours a day (Tr. 3246) and would work at home using the telephone if he had leads to follow up. This field representative rarely recorded overtime because it had to be made up in production (Monson 3247). The maximum number of cases he could do in a normal workday in compliance with Company procedures was 12 (Monson 3252). This field representative, in fact, averaged 17 cases a day, which he accomplished by various shortcut-

[141] "Yes, there was a pressure to get the reports done within the allotted time, and it was not generally favored if they were not done within that amount of time, and I did resort to not always interviewing the sources I had listed." (Tr. 4515).

[142] About 20 percent of her cases, when first received, were on the second, third or fourth day of Time Service. She received cases on the fourth day for the first time infrequently, however (Hille 4511).

[143] Her testimony on this point is not rebutted by respondent's computations in RX 424. These show that, in a 3-month period, June-August 1973, when her monthly salary was $605, the required number of cases per day to break even was 14.1, 14.1 and 15.2 (RX 424Z–19, Z–21, Z–23).

[144] Her average production per day, according to respondent's computations for the period June-August 1973, was 13.8, 14 and 16.1 cases (RX 424Z–19, Z–21, Z–23). Again, the divergence is insufficient to rebut her testimony.

[145] There is nothing in RX 424 which precludes a finding that, on some days, her actual production exceeded the daily average as computed in the exhibit in an attempt to make up for prior losses.

ting techniques, such as the use of the telephone (Monson 3252–53).[146] Sometimes, he would fabricate an informant "when there was pressure to get a case completed, and it was impossible to find a reasonable source of information, and [he] only had one to rely on, [then] the other one would be made up" (Monson 3254). This is a technique he used during a major portion of his time with respondent (ibid).[147] He faked sources two to three times a month (Monson 3299). To implement this technique, he used vague listings of sources which could not be traced (Monson 3300). In addition, this field representative might stretch the time a source had known the subject of the report in order to meet time coverage requirements (Monson 3300–01). [138]

387. A field representative in the Tucson, Arizona branch office needed 15 cases a day to meet his production requirements (Moxham 3497).[148] His actual assignments could vary from 10 to 20 cases per day (Moxham 3499). He was able to prepare 12 cases in an 8-hour day in accordance with Company rules and regulations (ibid, Tr. 3512). However, if he had completed only 11 or 12 cases for the day, his production would have to pick up because he needed 14 to 15 cases on the average (Moxham 3499). On occasion, he would list a source as meeting the time coverage requirements for a report, although the source had not, in fact, known the subject of the report for the required period of time (Moxham 3516–17). This field representative took circuit runs involving 30 cases a day (Moxham 3498).[149] His workday on the circuit averaged 10 to 12 hours (Moxham 3508).[150] Finding the subjects of the report and neighborhood sources in the outlying areas of this circuit was time consuming (Moxham 3508–09). He faked sources about 10 to 20 percent of the time on the circuit (Moxham 3515).

388. A field representative in the San Mateo office had to complete 16 single fee cases a day to cover salary and expenses, excluding dictation expense and bonus (Feriante 4428–29).[151] This field representative was unable to do 16 single fee reports on the average while following Company procedures. He varied from Company procedures by his use of the phone (Tr. 4435–36) and failing to ask the full range of questions in all instances (Tr. 4438).

[146] Forty percent of his cases were cleared, although not totally handled, on the telephone. Some cases he would complete solely through the use of the telephone (Tr. 3253).

[147] He fabricated more sources in his last month with the Company when he had two jobs, faking in approximately 40 percent of his cases at that time (Tr. 3254).

[148] With 15 reports, he was "a little bit in the clear," making some bonus; with 14, he would be slightly behind (Moxham 3497).

[149] The cases would be dictated the following day (Tr. 3498).

[150] The run was always more than 8 hours, although 12 hours was an extreme (Tr. 3515).

[151] Normally, it was necessary to take out more cases than that to complete 16 cases (Feriante 4429).

On occasion, 80 to 90 percent of his contacts were by phone (Feriante 4443). He also listed neighborhood sources not seen in his reports (Feriante 4440–41, 4444). **[139]**

389. Another field representative in the San Mateo office attempted to complete 18 full fee cases a day (Silar 3891). He was unable to prepare these cases in accordance with Company procedures (Silar 3911–12). This field representative varied from Company procedures by using inadequate sources, using fewer sources than required and in his use of the telephone (Silar 3912). He also listed sources not seen 75 percent of the time (Silar 3914).

390. A supervisor of a unit in the San Mateo office was unable to interview the required sources for his reports in the time available to him (Ledum 4702). He listed sources not seen (Ledum 4702). This field representative made the effort to interview all sources up to the fourth day that the report was in the office and then faked sources not seen in order to get the report out (Ledum 4701–02).

391. Respondent's officials admitted that, prior to the arrival of a new manager in January 1972, the San Mateo office was disorganized and not adequately supervised (Eldred 11163). And, that such conditions in the office had a negative bearing on field representative productivity (Eldred 11293).

392. The manager under whose direction such conditions arose held this position from 1969 to his termination at the beginning of 1972 (RPF 434; Tr. 13205).[152] The three field representatives from the San Mateo office testifying for the Commission (Findings 388–90) worked there during the entire period that this manager held office.[153] **[140]**

393. A part-time field representative in the Santa Monica branch office, in the period after April 1971, listed sources not seen (Milligan 4583–84). The faking of such sources in 1971 was a carryover of habits formed during his employment as a full-time field representative of respondent in 1970, when he was unable to do reports assigned to him in the time available (Milligan 4569–70).[154]

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[152] The vice president in charge of the region who held this job from April 1970, had become aware on his first visit to the office of poor morale in that office, but did not terminate the manager in question until the beginning of 1972 because, as a matter of fairness, he felt he should be given at least a year (Smith 13178, 13203–05).

[153] December 1962 to January 16, 1974 (Ledum 4642); June 1966 to March 1972 (Silar 3877–78, 4072); September 1962 to mid-February 1972 (Feriante 4413–14).

[154] He faked sources less frequently as a part-time field representative than as a full-time employee "because my case load was lighter and I could be more selective in the cases in which I would work which was a sore point with the salaried inspectors because they felt that they should be given the gravy and I should be made to go out and dig up the hard stuff." (Tr. 4570).

This witness estimated that, during his full-time employment, his production was "maybe" 12 to 14 cases a day (Tr. 4555–56). His actual production averaged less than eight single fee reports a day (Tr. 4574, 4590).

Field representatives under respondent's production system (not just Commission witnesses) not infrequently tend to overestimate the amount of the reports they do (Zack 8235–36, see also Brown 6969–70). One reason is that, on certain days, field representatives do handle a large number of cases (Zack 8236).

394. A field representative in the Newark office found there was not enough time to do the job in the normal workday (Buckley 1356). He attempted to do 12 to 13 cases a day at the beginning of the month (id.). This field representative only secured adverse or protective/declinable information at the beginning of the month when the pressures requiring volume production were less stringent (Buckley 1355). This field representative sometimes would not confirm adverse information as required through a second source (Buckley 1326), although two sources would be shown on his reports (Buckley 1348).[155] [141]

395. Field representatives were assigned circuit runs. The term "circuit run" refers to a trip by a field representative to a rural area where he visits several small towns or cities which are too sparsely populated or too far away from an office to permit the field representative to follow a normal schedule in handling cases. A circuit run is longer than a usual run (Jenkins 5786, Andrews 9420; see also RX 102Z-50).[156] Frequently, the circuit run was what was called a "double run" or two days' work (Crepeau 1756), where the field representative was given a large number of cases to prepare over 2 days. He would "spend the day on the run" investigating the cases and would dictate or type up the reports the following day (Andrews 9421-22, Kain 9460-61, Lieber 9069). As a general rule, field representatives on a circuit run worked more cases than in their regular local areas (Jenkins 5787).[157]

396. The number of cases in a circuit run could vary considerably, for example: [142]

Madison, Georgia Suboffice	25-50 cases[158] (Ivey 1999, 2009, 2011).
Tucson Branch Office	50-55 cases* (Jenckes 74-76, 100-01).
.....	30 cases* (Moxham 3498).

[155] When asked why he did not confirm adverse information, this witness stated that he did not have the time: "[t]here [are] so many reports to do to make the money that you have to make that when you go out in the field, assuming that you go out there and don't use the telephone, you just have enough time to make so many stops and if you have to get 2 sources or even 3 sources on a decline, if you don't get it from the first one, it is impossible to do your job, and there is no way." (Tr. 1347-48).

[156] *E.g.*, the average circuit run from the Appleton, Wisconsin suboffice involved a number of small cities and covered 100 to 200 miles (Pregler 9201-02). However, a circuit run from the Salt Lake office involved nine communities and covered about 350 miles (Huntington 12589-90).

[157] Similar to circuit runs were "relief runs", wherein field representatives from one office were sent to another office (branch or suboffice) with a backlog of cases, to assist in preparing reports (Brothers 7412-13). Field representatives could be given a larger number of cases than usual on relief runs and could work longer hours than usual (Lieber 9070).

[158] Mr. Ivey might work up to 13 or 14 hours a day if the workload on the circuit run was 50 cases (Tr. 2011).

Claremont, New Hamphsire Suboffice	50–80 cases* (Crepeau 1756).
New Orleans Branch Office	40–70 cases* (Laudumiey 1827–29).
Salt Lake City Branch Office	30–50 cases* (Huntington 12589, 12592).
Alexander City, Alabama Suboffice	40 cases* (Martin 12890–92)
	40–60 cases* (Jones 12916, 12919–20, 12935–36).[159]

*These circuit runs were double runs, *i.e.*, the investigation was handled on one day and dictation the next. [143]

397. Field representatives frequently used stock sources in the preparation of reports on circuit runs (Huntington 12591, Jones 12918, Crepeau 1758). A "stock" or "central" source is a person in a small town, typically a businessman or merchant, who can be used by a field representative as a source for numerous reports on a circuit run (Huntington 12591, Crepeau 1759).

398. Field representatives utilizing stock or central sources were cautioned:

A careful selection of good sources is one of the prime requisites of a good report. Do not depend on "stock" or "book" sources just because they know the subject of the report. Such persons may be excellent leads to suggest to you someone who is a logical source. Be sure that each source is in a position to give the necessary facts.
(RX 102Z–50.)

399. On circuit runs, field representatives tried to clear as many cases as possible using central or stock sources.[160] [144]

400. A field representative in the New Orleans branch who worked circuit runs of 40 to 70 cases a day in rural areas used stock sources. He did not ask such stock sources the normal questions since, in his view, such sources knew exactly what he wanted (Laudumiey 1828–29). The procedure of another field representative in obtaining information from stock sources was: "You knew them, and they knew what you want, and I just run the name through to

[159] Mr. Jones pointed out that he seldom completed all cases assigned during a particular circuit run (Tr. 12917; see also Larson 12523).

[160] A field representative in the Tucson office could complete 25 reports on a circuit run through three to four stock sources, if he "had any luck at all" (Jenckes 76). A field representative from the Claremont, New Hampshire office with double runs of 50 to 80 cases a day, generally cleared such cases by using central sources (Crepeau 1756, 1758–59). On a circuit run from the Alexander City, Alabama suboffice, a field representative on the average took 40 cases; on one of his runs, he would clear 20 cases solely through stock sources (Martin 12902).

Respondent emphasized the importance of interviews with applicants because applicants are considered the best sources of protective and declinable information (see Findings 315–16).

them, and if there was anything wrong with him, he would stop me and he would discuss it and clear it up" (Crepeau 1759).

401. Field representatives discussed with each other the prevalence in their office of such practices as faking sources or other shortcuts (Hille 4517-18; Silar 3924; Buckley 1255, 1257; Monson 3254-55, 3260, 3287). Field representatives in their conversations also expressed the view that the job was virtually impossible (Wines 390; Dodson 3069-70, 3067-68). The existence of such conversations demonstrates a state of mind in branch offices likely to lead to infraction of Company policy such as the falsification of sources.[161]

402. Generally, field representatives did not fake sources in those instances where unfavorable or protective/decline information was developed (*e.g.,* Monson 3302; Moxham 3515; Pollard 316, 356, 361; Feriante 4448-49 cf. Wallace 3014; Hille 4534-35).

403. Field representatives were subjected to conflicting pressures; namely, to produce a certain number of reports in a normal workweek and meet Time Service requirements and, at the same time, to produce protective/ declinable information by careful interviewing and by asking a full range of questions (see Findings 315, 344, 354-55, 372-74; see also Findings 370, 371). [145]

404. Many field representatives were able to complete the caseload assigned within a normal workweek in accordance with Company procedures and to earn a full or partial bonus; certain of them put in some overtime in earning the bonus (*e.g.,* Baranek 9703, 9698-99; Bender 7687-88, 7683-84; Getz 12348-49, 12397; Harroun 9512, 9506-07; Hilderbrand 12011-12; L. Jones 10454-55; C. Matthews 12788, 12795, 12803; Rawls 11065-66; Saltzgaber 11972-74, 11983-84).

405. A substantial number of field representatives, however, were unable to complete the work in either the normal workday or workweek in accordance with Company procedures. They compensated for such inability by contacting unqualified sources, faking sources, misstating time coverage, hurrying through interviews, failing to ask a full range of questions, using the telephone in a manner not in accord with Company procedures, or working excessive overtime (Findings 377-94, 400).

406. Respondent instructed its field representatives:

Honesty—Fairness

Our business has been built upon integrity and character; nothing in it is more

[161] Another field representative felt he could falsify sources when he saw reports prepared by others with vague listings such as "resident" and an address (Pollard 358).

important. As a service company, the nature of our business makes it essential that we maintain and adhere to strict principles of honesty.

In many businesses, the term 'dishonesty' implies mishandling of money or merchandise. We sell a service—therefore, such actions, for example, as recording hours not worked and miles not driven, or listing sources not contacted, constitute dishonesty in our type of business. For obvious reasons, anyone found lacking in honesty, in our strictest sense of the word, cannot be retained as an employee. [146]

There is no room for prejudice in our work. The person on whom we report is entitled to scrupulous fairness on our part. This obligation is co-equal with our responsibility to our customers as well as to our Company. You are not being fair to them unless you are also fair to the subject.

(RX 102D.)

407. It was respondent's policy to terminate immediately all field representatives falsifying information such as sources during the course of an investigation (RX 102D; Jenkins 5778, Lieber 9015, Browning 6062, Baranek 9703, Dodson 3096–97, Pollard 358, Ledum 4717).[162] This policy was communicated to respondent's field representatives and was generally carried out when such practices were detected (*e.g.,* Tr. 4717, Shaffer 8389, Burk 10380, Getz 12349, Curtis 7152–53).[163]

408. It is not possible for a manager or supervisor to determine whether all information was properly obtained and whether all sources listed were, in fact, interviewed simply by reading a report (A. Brown 7747, J. Curtis 7154, Freeman 10199, Hives 9735–36, J.F. Moore 10043–44, J. Moore 8842). Reading a number of reports prepared by a field representative may lead to a suspicion that there has been falsification. However, it is seldom possible to be certain from a reading of the reports alone. Vague source listings in a series of reports may raise a question as to whether all listed sources were, in fact, interviewed [147](Curtis 7154, Freeman 10199–200, J. Moore 8842, Brothers 7420–21, Lieber 9015–17). Reports consistently containing minimal amounts of information may raise the same question (Lieber 9015–16). And, respondent's management believes that the absence of protective and declinable information on a consistent basis may also indicate that sources have been falsified (Brothers 7420–21, Laugavitz 10328, Jenkins 5779–80). An excessive number of reopened cases (Jenkins 5778, Lieber 9016, Curtis 7153) may raise similar suspicions.

409. Respondent employs various measures such as the put-up system (Curtis 7153, Lieber 9016), the regular review process in the office (Lieber 9015), and analyses of field representatives' cases

[162] Two of the Commission witnesses testifying herein were terminated for that reason.

[163] There were some exceptions: see CX 1592A–H. In the Denver office, the discipline meted out depended "entirely on the degree of fabrication." In that office, falsification of time coverage, according to one of respondent's witnesses, apparently was not considered as serious as other infractions (Hilderbrand 12012–13).

covering such subjects as source listing, source selection and information content, to check the integrity of reports (Brothers 7375–77, J. Curtis 7146–47, Lieber 9034–35, Crawford 12568–69).

410. Performance reviews are conducted on trainees, and, periodically, on other field representatives and on an as-needed basis. They involve going on the street to recheck with the sources listed by field representatives in previously completed reports to determine that the sources were, in fact, contacted, that all the questions were asked, and that the reports accurately reflected the answers (Brothers 7377, Browning 6062–63, Curtis 7148, Jenkins 5701–02, Eldred 11202, Crawford 12568–69, Hilderbrand 12014). Performance reviews may be utilized when there is an indication the reports may have been falsified (Lieber 9016–17, Ross 9343–44). Performance reviews are a cost to the branch office (Bresnahan 567–68).[164] [148]

411. Respondent failed to effectively police falsification of sources by certain of its field representatives.[165] Its supervision must be deemed ineffective.

412. A substantial number of field representatives have falsified information such as sources (Finding 405). The widespread nature of this practice and the fact that such facts were committed by field representatives knowing they risked termination for such infractions compels the inference that a substantial number of field representatives were unable to complete the job assigned to them in a normal workday in accordance with respondent's instructions.

413. Such inability resulted from the fact that particular field representatives were given more cases than they could complete in accordance with Company procedures in the particular areas where they worked or under the conditions prevalent in the offices and areas to which they were assigned. Such inability led to shortcuts such as faking. Thus, respondent's investigative procedures may result and have resulted in inaccurate reporting. Certain field representatives taking shortcuts, such as falsifying sources or utilizing unqualified sources, may have been ill-suited for the job because of lack of competence, disorganization or personal problems. This evidences only that respondent has hired a substantial number of employees unable to cope with the workload and the working conditions generated by respondent's compensation system and other policies. Inaccurate reporting is likely where considerable

[164] Normally, it is computed on an hourly basis at the normal hourly investigative rate (Tr. 567).

[165] *E.g.*, faking sources 10 to 20 percent of the time on a circuit run (Tr. 3515). Faking sources 2 to 3 times a month (Tr. 3298–99); not interviewing sources listed about 75 percent of the time (Tr. 3063); listing sources not seen in 30 percent of the cases (Tr. 4514–15); listing outside sources not seen 40 percent of the time in those instances where a direct interview with the insured was obtained (Tr. 2870); faking sources on the order of one out of 15 cases (Tr. 356); faking by a long-time field representative known to management as "consistently sporadic in his work habits" (Tr. 455, 458, 460–61; RX 483A).

numbers of field representatives are unable to meet the requirements of respondent's system for whatever reason, notwithstanding the fact that others with more ability or more favorably situated are able to cope. [149]

C. Respondent's Computations Pertaining to Reasonableness of Compensation Procedures

(1) Respondent's 1969 and 1973 Product Cost and Effort Studies

414. Respondent has, from time to time, made product cost and effort or time studies to determine the effort required to complete various types of reports in different parts of the country (Burge 5012–13).

415. Analysts in respondent's research department used data from such studies for two major purposes:

1. To compute profitability by type of report, and
2. To develop standard cost estimates for proposed new reports. (RX 566 III–5.)

416. Time studies were conducted in 1967, 1969, and 1973 (Bruns 13912–14; RX 566).[166]

417. The 1969 time study had a goal of timing 5,000 reports and, in fact, 3,619 timings were completed in that study (Bruns 13914, Deibig 13614–15). Analysts conducting the study spent approximately 222 man-days in making observations in the field (RX 566 I–1). One hundred seventy field representatives out of a population of 6,031 were timed in the 1969 study (RX 566 II–11).

418. The scope of the 1973 study was more limited than the 1969 study. It included observations of approximately 1,500 individual reports. Analysts conducting the study spent approximately 151 man-days in making observations in the field (RX 566 I–1–I–2). Eighty-eight field representatives out of a total population of 5,145 were timed in the 1973 study (RX 566 II–11). [150]

419. The timers or analysts who conducted the 1969 and 1973 studies observed each field representative selected for inclusion in the studies for one full day. The procedures involved in such observations included the following major steps:

> The analyst worked with the manager of the office where he was to conduct observations to determine which field representatives were to be observed . . .
> The analyst met the field representative at the beginning of his day's work. He

[166] Since 1973, respondent has conducted timings in 1975 and 1976 (Deibig 13878).

then observed his activities throughout the day and timed each of the field representative's tasks with a stopwatch.

The analyst entered the stopwatch timings and other pertinent information on standard forms . . . .

(RX 566 I-5.)

420. For the 1969 study, respondent sought to select a representative group of offices per region, including larger metropolitan branch offices, smaller branch offices in the country and suboffices (Bruns 13938). Some consideration was also given to selecting offices not timed in 1967 (Bruns 13969).

421. In 1973, the branch offices to be timed were selected by respondent's employee James Deibig, who broke down all branch offices then existing into three categories: large, medium and small. Selections were made from the three categories, with an attempt to secure a geographic mix of all three types (Deibig 13623–24).[167] The study, however, was cut short and a number [151]of the branch offices and suboffices originally scheduled for timing were not timed. Respondent's witness responsible for selecting the cross section of offices was unable to state how many were dropped (Deibig 13631, 13866).

422. Field representatives chosen for timing were not chosen on a random sampling basis (RX 566 II-8–II-9).[168] Since random sampling was not used, the data obtained in the study cannot be relied upon on a purely theoretical statistical basis to make predictions about total population (Brown 14172–73, 14214).

423. Respondent described the procedures for selecting field representatives as follows in its exhibit, RX 566:

General guidelines were provided to the study analysts for requesting field representatives to be made available for timing by each branch office visited. The final decision as to which individuals would be timed was left to the analyst and the branch office manager.

. . . The study procedures specified that advance notice was to be given to the offices to be visited regarding the types of reports that should be covered in the timings. The analysts had been instructed to request individuals to be timed who would provide maximum coverage of the basic report types. The procedures specified that they were to avoid timing field representatives whose reporting standards reflected subsidies provided by the Company, and that they [152]should attempt to obtain timings for a cross-section of field representatives by length of service and by level of performance. These guidelines would tend to exclude from the study field representatives working primarily special, nonbasic reports. The guidelines would

[167] To cut down on driving time for the timers, an attempt was made to line up the three to four suboffices that the timers would visit each week within an hour's driving time of each other (Deibig 13878).

[168] For a sample to be random, the procedures used to select the sample from the total population must assure that each element in the population will have an equal chance of being selected for inclusion in the sample (RX 566 II-9).

also exclude high and low-performing representatives, since only trainees and management-level representatives have subsidized reporting standards. (RX 566 II–8.)

424. In fact, the field representatives to be timed were selected by the branch office managers (Tr. 13887, 14050).

425. Some of the more prevalent reports timed in 1969 were the regular life report, life NORS written, life NORS non-written, intermediate life, streamlined life, special narrative life, automobile, streamlined automobile, ballpoint pen auto, personnel selection, double rate personnel selection, and triple rate personnel selection (Deibig 13533).

426. In selecting cases to be timed in 1973, respondent's employee, James Deibig, listed 85 services which constituted "almost 90 percent of the total revenues produced by Retail Credit at that time." He excluded from these "target cases" those on which numerous samplings had been obtained in the 1969 study and provided tally sheets to the timers so that a minimum of 30 timings could be completed on each report scheduled for timing. Although regular life and regular auto cases were not targeted, timings of such cases were completed in 1973 due to "the nature of those two reports." (Deibig 13624–25).

427. On the basis of the 1973 study, respondent computed the following average effort in minutes required to complete its basic life and auto reports: [153]

	No. Cases Completed	*Average Effort (Minutes)**
Life	188	28.750
Auto	275	31.317
Normal Report Time (weighted average of Life and Auto)		30.275

(RX 566 III–7.)[169]

(2) Evaluation of the 1969 and 1973 Time Studies by Arthur Andersen & Co. (The Andersen Study)

428. Arthur Andersen & Co. (Andersen), respondent's outside auditing firm (Woodham 14094), was retained to review the procedures utilized by respondent in its time studies to gain an understanding of those procedures and to prepare a report giving

[169] Arthur Andersen & Co. recomputed the effort necessary to complete those reports and determined that respondent's computation had overstated the average effort per report. Its computation showed an average of 26.64 minutes and 28.75 minutes, respectively for the basic life and auto reports (RX 566 IV–14). The Andersen study (see *infra*), after adjustment, relied upon 191 observations of the regular life report and 273 of the regular auto report (RX 566 V–8, IV–15).

Andersen's evaluation of the procedures utilized (Tr. 14095). Andersen was also asked to examine the data from the timing sheets and to relate the findings from the study to the performance standards of the Company for field representatives (Tr. 14096). RX 566 is the study prepared by Andersen at respondent's request.

429. Andersen's stated purpose in making the review was:

—To gain an in-depth understanding of the purpose, scope, procedures, and results of the studies conducted in 1969 and 1973; [154]
—To evaluate the studies and identify any weaknesses in procedures and scope; and
—To perform additional analyses of the data obtained during the studies to determine whether the results support the reasonableness of the Company's field representative reporting standards.
(RX 566 I–13.)

The completed study was transmitted by Andersen's letter, dated May 30, 1975 (RX 566).

(3) Andersen Evaluation of Respondent's 1969 and 1973 Product Cost and Effort Studies

430. Work measurement is a systematic method of recording observations of work activity usually for the purpose of establishing or revising standards for performance in a job. It is generally employed in manufacturing or purely clerical situations where the worker location is fixed, where the task to be performed can be divided into small elements, and the task itself is repetitive and brief in duration (RX 566 II–2).

431. Andersen concluded that completion of investigative reports by field representatives was not a typical application of work measurement technique and that the basic steps followed by respondent would be expected to differ from those that would be followed in a manufacturing or clerical environment. It concluded further that basic work measurement concepts were, nevertheless, applicable (RX 566 II–2).

432. Respondent's product cost and effort studies, utilized for the purpose of determining how long it takes to prepare reports for the purpose of using the data to price the product were innovative at the time they were conducted (Prince 14476, 14478). Work measurement was being extended beyond industrial activities to service industries (Tr. 14477). In this connection, Andersen felt that respondent was on the leading edge of using work measurement techniques for such purposes (Tr. 14477).

433. Andersen concluded that, although the sampling technique used for selection of field representatives could not have resulted in a

random sample, the actual results [155]obtained appear to correspond reasonably well to the Company's total population of field representatives in terms of length of service with the Company (RX 566 II–9).

434. It is difficult to determine whether bias exists in the samples from a visual comparison of the length-of-service percentages in the samples to the total population of field representatives. Andersen, therefore, utilized a statistical test to determine whether the samples were biased. The results of the test did not indicate a biased sample in the 1973 study. The test did show a biased sample for the 1969 study with more field representatives timed in the 1 to 5, 5 to 10, and 10 to 15 years length-of-service groups (RX 566 II–9–II–10).

435. Andersen, in its review of the procedures used by respondent in conducting the product cost and effort studies, concluded that the techniques utilized were reasonable in relation to the studies' purpose and scope, and that they generally conformed to widely used work measurement techniques and that the timing data obtained could, therefore, be expected to be representative (RX 566–10). Andersen, subsequent to the completion of its study, RX 566, suggested that respondent, in future cost and effort studies, make changes in the selection of offices and field representatives to make selection procedures in further studies more objective and more mechanical (Brown 14417–18, Woodham 14110).[170] The revised procedure suggested makes use of random number tables for such selections (Woodham 14122–23). Andersen's recommendations in this respect have been adopted (Deibig 13751).

(4) Andersen's Analysis To Determine the Reasonableness of Reporting Standards (The Bonus Contribution Calculations)

436. Andersen chose monthly bonus contribution as a measure of the reasonableness of the field representative [156]reporting standard (Woodham 14108–09; RX 566 IV–7). Andersen determined that an 8-hour day, 40-hour week was a normal workweek and based its review on that assumption (RX 566 IV–6; Woodham 14108).

437. For the purposes of its study, Andersen defined Monthly Bonus Contribution as "the excess of earnings credit over salary and expenses that would be earned by a field representative with a given set of reporting standards and a workload consisting solely of a given type of report." (RX 566 IV–7).

438. Andersen determined at the outset of its review that the

[170] Andersen's "recommendation was that all subjective types of decisionmaking be eliminated whenever possible respecting [selection of] branch offices and field representatives" (Brown 14418–19).

scope of its analysis of the study results should be limited to the following basic type of reports offered by respondent:

—Regular Life
—Life-NORS Notification
—Auto
—Streamlined Auto
—Health
—Streamlined Life
—Life-NORS Written

439. These seven basic type reports were selected because life and auto reports represent the Company's largest volume of business and on the assumption that the seven basic type reports are those that comprise the typical workload for a field representative with 1 to 5 years of service with respondent (RX 566 I-13-I-14).

440. Andersen concluded that:

> The results of the analysis of bonus contribution shown on pages IV-24 and IV-25 [of RX 566] support the reasonableness of Retail Credit Company's field representative reporting standards. For the one to five year length of service and code 4 office reporting standard, the analysis shows a positive contribution to bonus for each of the seven types of reports. For the composite reporting standard, only report codes 27 and 9999 (Streamlined Auto and Life-NORS Written) show a negative bonus contribution. [157]Since these two types of reports are relatively low volume in terms of the Company's overall business, it is likely that any losses against standard resulting from the under-rating of these reports would be offset by gains against standard for the other reports in an actual field representative's mix of work.

(RX 566 IV-22-IV-23.)

441. Andersen's Table IV-24, RX 566, is an analysis of bonus contribution on the basis of the 1973 study for the 1 to 5 year length-of-service group in Code 04 offices. According to Andersen's calculations in that table, the following monthly bonus contributions are shown for the reports indicated:

Report	*Bonus Contribution*
Code 1 (Life)	$120
Code 20 (Auto)	93
Code 9 (Life-NORS Notification)	136
Code 27 (STRL Auto)	33

Report	*Bonus Contribution*
Code 115 (Health)	97
Code 133 (STRL Life)	158
Code 9999 (Life NORS Written)	77 [158]

442. Andersen's Table IV-25, RX 566, is an analysis of bonus contribution derived from the 1973 study calculated on the average for all lengths of service for all offices. According to Andersen's calculation in that table, the following bonus contributions are shown for the reports indicated:

Reports	*Bonus Contribution*
Code 1 (Life)	$29
Code 20 (Auto)	1
Code 9 (Life NORS Notification)	40
Code 27 (STRL Auto)	(66)
Code 115 (Health)	6
Code 133 (STRL Life)	63
Code 9999 (Life NORS Written)	(16)

443. The only test performed by Andersen to examine respondent's basic premise that field representatives are adequately compensated in preparing basic life and auto reports was the foregoing monthly bonus contribution analysis (Brown 14301).

444. The tables at IV-24 and IV-25, RX 566, contain the calculations on which Andersen based its original conclusion that field representatives are adequately compensated on the basic life and automobile reports. In reaching this conclusion, Andersen relied equally on both charts (Brown 14302-03). **[159]**

445. As a result of deficiencies concerning the exhibit brought out

in cross-examination of an Andersen witness, the schedule shown on RX 566 IV-24 was recomputed as RX 566 F, G and H.[171] Because of disclosure of the same data, Andersen determined that the chart, RX 566 IV-25, was invalidly computed and could not be relied upon for any meaningful purpose (RPF 623). Andersen did not recalculate RX 566 IV-25 "because upon learning of the different rates and reflecting upon the relationship of the variables involved it looked to us as if we would be drowning in a sea of averages anyway, [160]that the answer is not meaningful." (Brown 14448).[172]

446. RX 566 F, G, and H were substituted by respondent for RX 566 IV-24. Each deals with the computation of "bonus contribution" for the seven basic reports timed during the 1973 study.

447. RX 566 F computes bonus contribution for the 1 to 5-year field representative length-of-service group for field representatives in Code 04 branch offices in 1973, which branch offices had been assigned a Code 04 designation in 1972 (RX 566 F). With correction of one mathematical error, it is identical to RX IV-24 (Brown 14395-96, 14404-05; Deibig 14618).

448. RX 566G computes bonus contribution for the 1 to 5-year field representative length-of-service group for field representatives in suboffice locations of Code 04 branch offices in 1973, which suboffices themselves did not carry a Code 04 designation (RX 566 G; Deibig 14626).

449. RX 566 H computes bonus contribution for the 1 to 5-year field representative length-of-service group for field representatives

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[171] RX 566 IV-24 was prepared on the assumption "that there was only one rate [price of report] in effect for a Code 04 branch office in 1973." (Brown 14390-91, 14404). Mr. Brown testified that he "[made] a mistake [in] following the assumption that there was one rate in effect in 1973." (Brown 14446).

During the first day of cross-examination of Mr. Brown, it was suggested that a Code 04 office had more than one rate applicable to it in 1973 (Tr. 14296-98, 14301, 14308-10, 14391, 14404). Mr. Brown confirmed that fact in conversation with Mr. Deibig after conclusion of the first day's cross-examination (Brown 14379, 14393; Deibig 14615). Prior to the preparation of RX 566 in May 1975, Mr. Deibig had informed representatives of Arthur Andersen & Co. that there was only one rate in existence for the Code 04 office (Deibig 14615; Brown 14296-98, 14301, 14308-10, 14379-80; Woodham 14650-52). In 1975, Mr. Deibig did not recognize that there was more than one rate (Deibig 14616).

In 1973, respondent reduced the number of standard codes from seven to five and in so doing, respondent took what previously had been designated as Code 02 offices and suboffices and included these offices within the standard Code 04. Former Code 04 and former Code 02 offices were both given the 04 designation (Deibig 14616-17, Brown 14379-81).

[172] The calculation on RX 566 IV-25 was based on the assumption as was the original RX 566 IV-24 that there was only one rate (price per report) for Code 04 offices in effect during 1973. Once it was determined that assumption was erroneous, the calculation on IV-25 was no longer viable. The introduction of a variable in the rate created additional variables with respect to factors such as salaries and expenses making it impossible to come up with "reasonable numbers." It was impossible, furthermore, to recalculate RX 566 IV-25 as was done in the case of IV-24 because it was impossible to compute an average salary for the entire company (Brown 14412-13). And, there was no average rate to correspond to the average salary (Woodham 14671).

in Code 04 branch offices in 1973, which branch offices had been assigned a Code 02 [161]designation in 1971–72 (RX 566 H).[173]

450. Andersen's monthly bonus contribution calculations per type of report were made on the assumption for the purposes of the computation that the field representative does one type of case everyday and completes the same number of cases everyday (RX 566 IV–7–8).

451. The Andersen analysis of bonus contribution, based on the average effort and mileage for all field representative length-of-service groups, rests on the assumption that any differences in the averages among length-of-service groups as to those factors are so small that they can be ignored (RX 566 IV–23; Brown 14253–54).

452. Respondent's branch offices were given different classification codes to reflect differences in the difficulty factor and costs in different areas, as well as differences in prices charged to customers for reports. The number of codes and the classification of given offices within the codes have varied over the years as conditions change (Case 5317, 5326–30). Between 1971 and 1976, the number of codes varied from five to ten (Case 5462–63). The difficulty factor in preparing reports is a primary consideration in designating a branch office's classification code (Case 5329).

453. Andersen's conclusions as to the reasonableness of the reporting standard is based on several factors including the assumption that Code 04 offices are [162]representative of respondent's organization[174] (Woodham 14673). Andersen's conclusion also relies on the assumption that an analysis of field representatives in the 1 to 5-year length-of-service group is appropriate to the evaluation of bonus contribution (Woodham 14673–74).

454. Andersen only wanted to give one example and not one for each code (Deibig 13748).

455. Andersen performed no calculations with respect to monthly

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[173] RX 566 F, G, and H each reflect computations based on a different report rate (Brown 14405–06). The report rates were obtained from RX 715. *E.g.*, the life rates of $4.85, $4.95 and $5.35 are found on RX 715D. Field representative revenue was also obtained from RX 715. For example, the field representative revenue credit of $4.85, $4.95 and $5.35 is found in RX 715M (Brown 14406–07).

[174] Andersen's computations in RX 566 IV–24 and RX 566 F-H were based on the assumption that respondent's Code 04 office was the branch office that most typically represented respondent's corporate averages of branch offices. Andersen consulted Mr. Deibig concerning the conclusion on RX 566 IV–24, which demonstrates a bonus contribution for the 1 to 5-year length-of-service group in a Code 04 office (Deibig 13747). Andersen asked Mr. Deibig to determine, based on his knowledge of respondent or of records of respondent, what the most representative code office would be. "Based on documents already submitted, primarily RX 754, we suggested to them that they use the Code 04 offices that most represented the averages of the company." (Tr. 13478). However, with the inclusion of the old Code 02 office, the 1973 Code 04 office, taken as a separate group, was not as close to being a representative branch as was the former Code 04 office in 1971 and 1972 (Deibig 14617).

bonus contribution in connection with the 1969 study results (Brown 14262).[175] [163]

456. With the repudiation of the chart on RX 566 IV-25, there is no calculation in the record showing bonus contribution for field representatives for all lengths of service for all offices.

(5) The Representativeness and Relevance of Respondent's Product Cost and Effort Studies and the Andersen Bonus Contribution Analysis

457. A representative sample is one that reflects the characteristics of the population being studied (Goldstein 15427).

458. The representativeness of the sample in a study is related to the question of how one can generalize survey results to the particular population under consideration (Goldstein 15341-42). Making a sample representative is a goal, and there are procedures which make it more likely that the goal will be achieved (Goldstein 15343).[176] One of the best procedures for achieving representativeness in the sample studied is to use random sampling procedures (Goldstein 15348, 15352):[177] [164]

459. Respondent did not utilize random sampling procedures in its time studies (Finding 422).

460. There are many variables bearing on the time required to prepare a report.[178] "For example, one variable that may be a factor, more important than age [length of field representative's service] would be the geographic location. Are there differences in geography between big cities, small cities? Are there differences between the scheduling techniques? Some offices have different scheduling techniques than others. And to sort out all of those variables and do an analysis to find out why is a very large undertaking." (Prince 14578).

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[175] An Andersen witness testified that, in his opinion, the conclusion would have been the same (Brown 14262). In fact, there are no calculations in this record on which findings on this point can be made.

[176] If it is desired to ensure the inclusion of a particular factor in a study, the variable may be stratified (*e.g.*, a particular type of organization) and a random sample taken within the variable (Goldstein 15348-50).

[177] Complaint counsel request a finding, based on a test for skewness by one of their experts, that the figures in the histogram at RX 566 IV-17 pertaining to effort for the life reports have less than one chance in a million of constituting a random sample from a normally distributed population (CPF 820). The finding is not adopted. To make the skewness test, one must assume that the figures tested are a random sample from a normally distributed population (Tr. 15678). Consideration has been given to Mr. Prince's testimony with respect to the histograms in RX 566 at Tr. 14508-09. This testimony does state the histograms contain a textbook distribution as complaint counsel contend (CPRF 1283). However, it is not clear whether this also means that the general population of life reports from which the sample is taken is normally distributed. Dr. Bartlett's comments at Tr. 15707 with respect to Mr. Prince's testimony are too general to permit a finding on this question. The witness was unable to state that life reports constitute a normally distributed population (Tr. 15707, 15717).

[178] " . . . One of the things that intrigued me is that there are so many variables in this whole task of preparing a report, the characteristics of the report, scheduling techniques that are used, there is a possibility of geographic location affecting it, the time of year, the mix of business, whether it is high volume or low volume, there are just a whole series of things here." (Prince 14548-49).

There was no analysis made of the impact of these variables (Tr. 14578–79).

461. The failure to analyze such factors was one of the primary areas where Andersen suggested improvement in respondent's time study procedures (Prince 14548–49).

462. Respondent's time studies did not follow generally accepted procedures in the sense that they left too much opportunity for bias in the selection of the offices timed and should have been more mechanical (Goldstein 15385).

463. The one manager testifying on this point stated that his selection of field representatives to be timed was based on considerations of volume, availability of the field representative, types of reports desired and field representative ability to do the reports. By availability, he meant selecting field representatives from units in which the work was light (Monarch 8567, 8579–81). This manager also selected one field [165]representative, because the stopwatch might demonstrate to this employee, one of the slower workers, where his time was going (Monarch 8580–81).[179]

464. The selection of field representatives from units with a light workload, for the convenience of the office, was not a criterion for selection spelled out in the instructions (see RX 765). Utilizing selection criteria not within the variables set forth in the instructions is contrary to standard procedure, and it is not possible to determine the effect of such a variable on the study results (Goldstein 15475).[180]

465. Respondent's selection procedures for choosing field representatives to be timed were not in accord with generally accepted procedures, since choices could be influenced by the manager's individual bias (Goldstein 15387).[181] [166]

466. The test by Andersen showing no bias as to selection in terms of length of service would not permit conclusions regarding the existence or lack of bias with respect to other variables such as

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[179] Field representatives were selected by this manager from those units which may have been light in volume because that would make it convenient for such persons to work with the timer (Tr. 8567). The record does not show why field representatives from a unit with a heavy volume would have been less available.

[180] Procedures should not be changed because of the study. This is basic to any kind of research. "You just don't do that. You don't want to be measuring the effects of your study. You want to be measuring the organization." (Goldstein 15482).

[181] ". . . [S]ince the manager can make the choices, he could make it according to any set of biases he might have. And certainly it is not a random selection procedure and the manager could, for example, select the best employees or the worst employees or a particular employee that he wanted timed for his or her own purposes or whatever." (Goldstein 15387; see also Tr. 15594–96).

This criticism by the Commission's expert, Dr. Goldstein, is confirmed by the testimony of the one manager testifying on this point that he selected one of his slower employees so you could show him where his time was going (Finding 463). In short, the testimony of this witness tends to confirm the position of Dr. Goldstein that the sample may have been influenced by the manager's bias in making the selections (Goldstein 15427).

ability of the workers, speed of workers or representativeness of the tasks timed (Goldstein 15424–25, Bartlett 15650–52).

467. In asking for types of reports, the timers concentrated on lines of reports for which they did not have an adequate number of timings (Bruns 13961). And, near the end of the 1969 study when certain cases were hard to find, the timers emphasized the need for those cases to the branch managers (Tr. 12964).

468. A timer in the 1969 study in three or four offices "just took the normal run of cases that an individual [field representative] had. . . ." When informed by the home office that a sufficient number of certain types of reports had been timed but others were lacking, the timer would "ask the manager [in other offices] to save those cases. . .the type of cases [he] would like to work on when [he] arrived at the office." (Healy 14028–29).

469. As a result, the selection of the cases to be timed in different offices was made on an inconsistent basis (Findings 467–68).

470. The holding of cases for the timing run means that such a run would not be the person's normal work and to that extent, it would be unusual. It is not possible to determine the effect of such practices on performance in the timing runs (Goldstein 15404).

471. Instructions to branch managers in 1969 and 1973 indicated that double runs or long circuits should be avoided (RX 765, 766; Tr. 13613).[182] Circuit runs and double runs constituted an important part of the work of [167]many field representatives (see Findings 395–96). The attempt in the instructions to branch managers (RX 765, 767) to exclude double and circuit runs tended to exclude from the sample variables significantly influencing the conditions under which a field representative works.

472. If normal performance is sought, it is important to ensure that the worker being timed knows that he is not being evaluated (Goldstein 15346, 15355–56).

473. Certain of the managers asked timers questions concerning the performance of field representatives in their office being timed (Bruns 13926, Healy 13998). Managers who asked such questions may have misconstrued the purpose of the study as permitting evaluation of individual field representatives (see Finding 463).

474. A timer in the 1969 study was occasionally asked by field representatives he had timed how they had done. He replied, "Nebulously. We would tell them they did well but we have not

[182] The actual practice in 1969 may have been contrary to the instruction (Tr. 13970). To the extent that there was a departure from the instructions, there is a possibility that inconsistent selection procedures may have been applied.

worked up figures so we can't really tell them how they compared to anybody" (Deibig 13880).

475. One field representative, after the timing, asked the timer how she had done:

Q Did Mr. Deibig, or anyone else ask you what your reactions were to the timings after you were completed?
A I was curious to know how I stood insofar as how my time was spent. I did ask him.
Q What was his response to you?
A He said I was very average. I said I'm sorry.
Q Why were you interested in how you stood?
A I just wanted to know how I did.

(Jerome 9684.)

[168]Such testimony indicates that the field representative may have been under the impression that she was being evaluated (Goldstein 15441–43).

476. Use of the production stamp, which indicated which field representative had prepared a report, may have given field representatives the impression that they were being evaluated (Goldstein 15574–75).

477. Debriefing of the subjects being timed is a procedure which may be used to determine whether a normal day's work was performed. It can cover topics such as whether the individual timed felt that he performed differently because of the study (Goldstein 15367–68). Absent a debriefing procedure, it is difficult to make a finding as to whether field representatives' subjective reactions to the fact that they were being timed affected the results.

478. Andersen's bonus contribution calculations are confined to Code 04 offices (Findings 445–49). The recomputation of RX 566 IV–24 set forth in RX 566 F, G and H demonstrates that there is significant disparity among subcategories of respondent's offices in the Code 04 classification with respect to the bonus contribution factor.[183] Thus (on the basis of Andersen's reasoning), [169]there is variation in ability of field representatives located in different

[183] For example, in the case of life and auto reports, the Andersen study showed the following variations with respect to bonus contribution:

	Life Reports	*Auto Reports*
Code 04 Offices which were Code 04 Offices in 1971–1972, RX 566F	120	93
Code 04 Offices Suboffice Rates, RX 566G	59	36
Code 04 Offices which were Code 02 Offices in 1971–1972, RX 566H	40	18

subcategories of the Code 04 offices to meet production requirements with respect to the same reports.

479. Andersen determined that Code 04 offices most typically represented respondent's corporate averages. In this connection, Andersen relied primarily on information received from respondent's employee James Deibig and RX 754 (Finding 453; Deibig 13748, Brown 14311). Andersen took no steps to test respondent's continuing assumption that Code 04 offices represented the Company's average office (Brown 14311).

480. RX 754, entitled "Production and Earnings of U.S. Inspectors," gives for 1971 and 1972 average production, revenue, reporting allowance, earnings (salary, overtime, gain-loss on standards) and expenses for field representatives by class of office. In 1971 and 1972, respondent had offices classified as Code 01, 02, 03, 04, 05, 06 and 07 (RX 754). See the following charts: [170]

PRODUCTION AND EARNINGS OF U. S. INSPECTORS

JAN-DEC '71	LOCAL INSPECTORS U.S. 1971							Total Local	Sub-Office	Grand Total
	01	02	03	04	05	06	07			
Productions:										
Reports	428	406	348	393	353	362	362	385	410	394
Revenue	1952	1840	1814	1886	1785	1832	1833	1871	1934	1884
Reporting Allow: Std. Per $	.435	.516	.541	.514	.534	.551	.544	.520	.491	.510
Amount	947	949	981	969	954	1009	997	972	950	963
Earnings:										
Salary	643	665	687	681	685	726	684	684	654	674
Overtime	14	15	14	14	12	13	12	13	15	14
G.I. On Stds.	62	67	65	67	63	71	79	67	64	65
Total	739	747	766	758	760	809	775	764	733	753
Expenses:										
Carfare	131	114	121	120	111	106	127	118	134	122
Steno	87	88	94	91	83	94	92	90	83	88
Other										
Total	208	202	215	211	194	200	219	208	217	210
Total Earnings and Expenses	947	949	981	969	954	1009	997	972	950	963

1971

PRODUCTION AND EARNINGS OF U. S. INSPECTORS January - December

JAN-DEC '72	LOCAL INSPECTORS U.S. 1972							Total Local	Sub-Office	Grand Total
	01	02	03	04	05	06	07			
Productions:										
Reports	427	402	392	374	334	325	326	394	409	398
Revenue	1990	1873	1847	1837	1815	1853	1870	1701	1867	1867
Reporting Allow: Std. Per $	499	529	555	529	548	526	557	534	505	525
Amount	993	990	1002	1019	1001	1026	1053	1017	993	1011
Earnings:										
Salary	691	692	719	714	717	717	716	716	681	705
Overtime	12	14	14	15	12	13	15	15	17	14
G.I. On Stds.	73	75	73	75	71	72	74	76	73	75
Total	776	781	806	804	800	802	805	807	771	794
Expenses:										
Carfare	125	110	130	123	114	120	130	119	139	126
Steno	92	88	96	92	84	92	94	91	89	90
Other	–	–	–	–	–	–	–	–	–	–
Total	217	198	226	215	198	212	224	210	228	216
Total Earnings and Expenses	993	990	1032	1019	1001	1014	1029	1017	999	1011

RX 734

[171]481. RX 754 demonstrates considerable disparity between the figures for certain classes of offices and both the Company averages and the Code 04 figures, with respect to the foregoing factors; *e.g.,* consider the Code 01 offices.

482. The variations shown on RX 754 with respect to the averages for factors such as production, earnings and expenses among various classes of branch offices also suggests that reliance on RX 566 F–H for generalizing to all of respondent's offices ignores significant differences from corporate averages with respect to such variables in the case of certain offices not in the Code 04 category.[184]

483. Andersen's bonus contribution calculations for Code 04 offices utilize an average salary of $610 and a reporting standard of .505[185] (RX 566 F–H). The reporting standard, however, varies sharply in different branch offices and for field representatives in different length-of-service groups (see RX 754, 715Z–3). The interaction of the per dollar standard or reporting allowance with salary is a critical element in the computation of bonus contribution (RX 566 IV–4, IV–5; [172]see also Tr. 14318–19).[186]

484. The Andersen study made no calculations as to the impact on bonus contribution of the interaction of reporting standards and salaries at ranges different from those shown in RX 566 either in connection with the computation for Code 04 offices, RX 566 IV–24, or for the composite of all offices, RX IV–25[187] (RX 566; see Tr. 14318–20).

485. Nor was there any attempt to determine how many field representatives might be required to meet expenses at a higher salary than shown on RX 566 (Tr. 14318).

486. As to these characteristics, therefore, there is insufficient evidence to show that the averages in RX 566 are applicable throughout the Company. [173]

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[184] In this connection, see respondent's statement, "With the inclusion of the Old Code 02 office, the 1973 Code 04 office, taken as a separate group, was not as close to being a representative branch as was the former Code 04 office in 1971 and 1972." (RPF 634). Mr. Deibig stated with respect to the consolidation of the Code 02 and Code 04 offices into one group, "it would have been my opinion that it would not have been as close—*if at all*—to the most representative in 1973, with the inclusion of the old 02 offices." (Tr. 14617; emphasis supplied). Moreover, a prime consideration in assigning a code designation to a branch office is the difficulty factor in preparing reports (Finding 452).

[185] The reporting standard for 1 to 5-year field representatives in Code 04 offices in 1973 (RX 715Z–3).

[186] Earnings credit is computed by multiplying the reporting standard by the field representative's revenue credit. Earnings credit is then matched against salary and other expenses to determine bonus contribution (RX 566 IV–4–IV–5).

[187] For example, if salary goes up and per dollar standard remains constant and assuming the same mix of cases, the field representative would have to complete more cases to achieve a given level of bonus (Tr. 14319). Conversely, if salary remains constant and per dollar standard goes up, the field representative would have to produce fewer cases to maintain constant bonus contribution (Tr. 14319). If both rise, it is clear that the relative rise in each would have an impact on bonus contribution.

(6) Significance of the Andersen Study and the Underlying Product Cost and Effort Study

487. The need to abandon one of the two basic calculations pertaining to monthly bonus contribution on which Andersen rested its conclusion as to the reasonableness of the reporting standard and the need to recompute the other, detracts from the confidence to be placed in RX 566 and the conclusions expressed therein.

488. Andersen's evaluation concerning the reasonableness of the reporting standard and the underlying time studies failed to take into consideration numerous factors bearing on the ability of the field representatives to complete their tasks in a given time (Finding 460). As a result, Andersen's studies fail to take into consideration that different groups of field representatives, because of variables such as geography, scheduling, etc., may differ significantly in their ability to complete a certain number of reports in a normal workday or in their ability to show a gain in any specific period.

489. The failure to analyze the impact of these variables makes it difficult to determine whether the conclusions of RX 566 are attributable to the entire organization or whether there are offices or groupings of offices to which they would not apply.

490. Andersen's conclusion, based on its bonus contribution calculation, that respondent's reporting standard is reasonable rests on the assumption that Code 04 offices are representative of the entire organization. That assumption has not been persuasively documented. For example, see disparity for bonus contribution within the Code 04 category for the various reports as calculated by Andersen for subcategories of the 1973 Code 04 offices as shown on RX 566 F–H (Finding 478). In addition, the Code 04 offices were selected as the most representative because averages for offices in this classification pertaining to such figures as production revenue and reporting standards were closest to companywide averages. [174] However, the pertinent averages for offices in certain other code classifications differ significantly from both the companywide averages and from those of the Code 04 offices (Findings 480–81).

491. Also, the bonus contribution computations failed to analyze the interaction of salaries and reporting standards at levels different from those shown on the computations in RX 566 (Finding 484). There is, therefore, in the case of these characteristics, insufficient evidence to support a finding that respondent's field representatives as a group were sufficiently homogenous so that the averages in RX 566 could be applied generally to them throughout the organization.

492. The purpose of the cost and effort studies was not to

determine the quality of the reports but to determine how much it actually cost to do the reports the way they were being done (Deibig 13764, 13781).[188] They were, accordingly, not designed to evaluate the effect of respondent's compensation system and other policies on the manner in which field representatives conducted their investigations. Since the time studies were not designed to study the quality of the reports, they have little relevance to the issue of whether respondent's procedures were designed to assure maximum possible accuracy of the information concerning the individuals to whom the report relates. [175]

493. The foregoing factors are relevant to weighing the conflict between the conclusions in RX 566 and other evidence. Under the circumstances, the testimony of certain ex-employees that they could not complete their workload in accord with Company procedures in a normal workday or week is entitled to more weight.

D. Production Credit for Reinvestigations

494. Respondent conducts reinvestigations on its reports when the accuracy or the completeness is in question (R. Jones 5177, Curtis 7150). There are three distinct categories of reopen cases: customer reopens, consumer reopens and office reopens (RX 107Z–170).

495. Reinvestigations are usually requested to clarify points of disputed information. As a result, it may not be necessary to rework the entire report (J. Moore 8850, 10038; Ross 9352; Curtis 7149; Zack 8894). Reopens do not deal solely with unfavorable information but they also deal with items such as birthdates and addresses (R. Jones 5176).

496. Respondent's policy in assigning reports for reinvestigation is the following:

> Generally, if the point in question is factual, and can be definitely resolved, age, duties, identities, marital status, etc., the original Field Representative should rehandle. *If the point is subjective and/or a difference of opinion is possible as to severity, degree of importance, health habits, reputation, an alternate Field Representative should be used.* In either instance, file copies should be withheld (original sources may be shown on Form 640) to assure objectivity.
> (RX 107Z–170; emphasis supplied.) [176]

497. When a reopened case is assigned to an alternate field

[188] "We [the timers] were not interested in what he [the field representative being timed] was saying or in the way he was asking his questions, therefore, the only requirement placed on us as timers were that we had continuous line of sight with the man up to the point he might enter a private residence. . ." (Deibig 13520). Since the timers did not hear the interviews, it would have been difficult for them to determine whether a field representative, in his questioning of sources, was more thorough than field representatives generally (Deibig 13765). And, normally, the timers could not determine whether the field representative being timed had asked a full range of questions (Deibig 13527; see also Healy 14020).

representative, he does not see the original report and he handles it as a new case (A. Brown 7774–75, 7888).

498. Branch managers are given discretion in the assignment of cases for reinvestigation on the ground that it is not possible to cover every contingency that may arise (Jenkins 5702). Exercise of such discretion varied, *e.g.,* in the suboffices, it was not, according to respondent's officials, always possible to assign a reinvestigation to an alternate field representative (Paladino 8738–39). However, if the circumstances were sufficiently serious, the branch manager might send in an alternate field representative from another office (Tilden 11780). And, in the Boston and Hartford offices, 99 percent of the cases were given to the field representative who handled the original report (Hakey 1658, 1730–31).

499. The rules for giving field representatives production credit for reinvestigations vary depending upon whether such reinvestigation is assigned to an alternate field representative or to the original field representative and whether or not the customer is charged for the new report. Respondent's customer is charged for a report when it reopens a case and the original information is confirmed (Hakey 1658–59, Laudumiey 1848–49, Silar 4029–30, Wallace 3014).

500. When the reinvestigation is assigned to a field representative who did the original investigation, he receives production credit for a customer reopen if the customer is charged for the reinvestigation; *i.e.,* if the original report is confirmed as correct (Lieber 9012–13, Curtis 7173, Moore 8850). If the reinvestigation shows an error in the original report so that the customer is not charged, then the manager has discretion as to whether to give production credit to the original field representative for rehandling the case (Lieber 9012–13, Paladino 8754, Moore 8849). [177]

501. The manner in which branch office managers exercise their discretion in compensating the original field representative for a reinvestigation when the first report was in error varies from manager to manager. Certain managers do not give production credit to original field representatives when the first report was in error on the ground that this would reward respondent's employees for improperly doing their job (Curtis 7293–94, Brothers 7439). Other managers give the credit as a matter of course (Larsen 12503–04, 12525–26). Some managers give production credit to such field representative if the error in the original report was not his fault (*e.g.,* J. Moore 8849–50, Paladino 8753–54).

502. In the event that an alternate field representative handles the reinvestigation, then that field representative receives produc-

tion credit whether or not the customer is charged (*e.g.*, Curtis 7173, Case 5414).

503. Normally, when a field representative receives credit for a reinvestigation, he receives the same credit provided for the original report (Zack 8895, Ross 9387–88, Larsen 12527). Where the reinvestigation requires more effort than usually required for the particular type of report, the field representative may, at the discretion of the branch manager, be given additional credit for such work (Zack 8895, Larsen 12506).

504. When field representatives are compensated for a reinvestigation and the customer is not charged, the equivalent revenue is deducted from the branch office revenue (Case 5413–14).

505. Respondent's failure to give production credit if the original report was incorrect, has the following effect in the case of some field representatives:

> Oh, in some instances where you would reinvestigate, you may find that the customer is partially right and you are partially right and in writing up this case, you would be inclined to more emphasize, put more emphasis on the [178]information showing you were correct so you could recharge the customer.

(Silar 4030.)

506. Another field representative was influenced as follows by the method of compensation for reinvestigations:

> Well, on reinvestigations, I would really—on those cases I would really try to really dig into it and I would try to prove that I was right the first time so I'd get my $5 but if it turned out that all wasn't true, I wouldn't lie about it. I would still tell the truth, that, well, I was wrong.

(Wallace 3015.)

507. The failure to give production credit for reinvestigations where the original field representative could not substantiate his original report clearly has potential to give field representatives an incentive to try to prove that they were right the first time (Findings 500–05). There is a danger that, in those areas involving subjective judgment on the part of the field representative and where differences of opinion are possible, there would be a tendency to deny the consumer the benefit of the doubt (Findings 496, 505). This point is tacitly recognized by respondent's Branch Manager's Manual (RX 107Z–170). However, no definitive finding can be made on the point. The record does not show the extent to which matters involving subjective points and/or where difference of opinion was possible were assigned to field representatives preparing the original report (see Finding 498). Nor does the record show with any degree of specificity any breakdown on how managerial discretion with

respect to granting production credit was exercised in such cases. The potential for inaccurate reporting is evident where the question in issue is subjective, and the reinvestigation is assigned to the original field representative, and where the manager, as a matter of policy, will not give production credit if the reinvestigation turns up [179]error in the original report. There is insufficient detail, however, in this record to determine that a pattern of inaccurate reporting has taken place by virtue of such compensation policies.[189]

E. Health and Arrest Information

(1) Health Information

508. Respondent obtained health information concerning an individual from sources other than licensed physicians, medical practitioners, hospitals, clinics or other facilities. Certain of respondent's reports require that the field representatives obtain such information from lay sources (Stansbury 6751–52, Jenkins 5793, Maust 8289, Hakey 1632, Wines 406, Monson 3274–75, Laudumiey 1838, Wallace 3005; *e.g.*, see CX 422A & B; RX 343A & B; Getz 12387–88).

509. Health information is to be confirmed either by the applicant or by two outside sources (Getz 12388, Hakey 1632–33, Laudumiey 1838, Moxham 3525, Pollard 328). The information in the reports is identified as coming from lay sources or the applicant (Moxham 3526–27, Muth 9954, Monson 3309).

510. Respondent considers the applicant to be a prime source of health information (Coleman 7954, Farra 755–57).

511. Although a neighbor cannot provide the doctor's diagnosis of a specific ailment, a neighbor may provide information which is generally known or derived from his observation of the applicant (Muth 9949). [180]

512. Field representatives were not required to confirm health information secured from lay sources through medical records (Wines 406–09, 411; see also Pollard 328, Buckley 1260, Monson 3275).

513. Underwriters do not take action based solely on health information obtained from lay sources in a report from respondent (Moller 13056, Jenkins 5793–94, Nietzold 13012, Paine 13396–97, Taylor 10841), but use such health information as a lead to request further information from medical sources, the agent or the applicant (Nietzold 13010–11, Moller 13055–56, Paine 13397).

[189] Complaint counsel cites one specific example where this may have occurred (CPF 965). However, that evidence was not allocated to these allegations of the complaint and must, therefore, be rejected on that score.

514. The record does not support a finding that health information secured from lay sources is inherently unreliable (Grossman 4199-4200; see also Elmendorf 4264). The testimony bearing on the issue is equivocal.[190] [181]

(2) Arrest Information

515. Respondent's field representatives, to complete certain reports, obtain information concerning applicants' arrest records (CX 422A & B; Jenkins 5794-95, Hakey 1633).

516. Field representatives are encouraged to check police records where available or where there is reason to believe that an arrest record on an applicant exists (RX 102Z-16-17).

517. Where it is not possible to confirm arrest information through police records, respondent's employees are instructed as follows:

> It is also pertinent to mention at this time the reporting of 'unconfirmed adverse information.' Example: If we develop information that there have been arrests, indictments, or convictions, but local police records are not available for confirmation, *WE SHOULD STILL REPORT THE INFORMATION.* But, when reporting the information, put it in the same language as we developed it, such as, 'there is talk in the community that your subject has had police difficulties, but police records are not available locally to verify this information.' It is important, however, that the approximate date of the difficulty be estimated and recorded because of the seven year requirement imposed on reporting adverse information.

(CX 1351I.) [182]

518. In certain jurisdictions, police records are not generally available (Curtis 3279, Jenkins 5795). In such instances, an attempt will be made to confirm the information concerning arrest through newspaper clippings or by interview with the applicant or a member

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[190] Dr. Grossman, one of complaint counsel's medical experts, testified that a "yes" or "no" answer could not be given as to whether neighborhood sources are likely to have accurate information as to the existence of certain medical conditions (Tr. 4199-4200). When asked whether it was reasonable for a field representative to obtain information concerning an illness from a lay source, he stated:

> A. I don't know how he would ask, but I mean the thing is in some situations the neighbors do discuss with each other conditions that they have and in other situations they do not; and neighbors often imagine things and, in turn, have gotten things in the record sometimes out of malice, so you have a mixed bag there. I mean you can't give one general answer for the whole thing.
>
> In some situations, I mean the neighbor might have, and in others it might suggest things that you may not want, and so *you really have a mixed bag there. I don't think you can give one answer to that whole situation.* The thing is the investigator can't differentiate what situation he is stepping into.

(Tr. 4199; emphasis supplied.)

Similarly, the testimony of Dr. Elmendorf, who stated there were better ways of getting information than from lay sources (Tr. 4261), did not give conclusive evidence on this point. He also testified that it was conceivable that it may be necessary to get information from neighborhood sources or other sources in connection with an insurance transaction (Tr. 4264).

Even accepting CPF 979-80, the one incident cited would not support a finding that securing medical information from lay sources without further confirmation is inherently unreasonable.

of his family (Curtis 7238–39, Hakey 1633) or through additional outside sources (Hakey 1633, Laudumiey 1840, Monson 3277). If lay sources such as neighbors or the applicant are used as sources for arrest information, the report will so indicate (Laudumiey 1839–40).

519. Some field representatives, if they were unable to confirm arrest information through police records, would not report it (Pollard 330–31).

520. The record contains no evidence pertaining to the use or accuracy of arrest information obtained through lay sources in specific instances. Nor is there other evidence bearing on the question of the reliability of such information. No finding can be made on the state of this record that respondent's practice of securing information of this nature through lay sources is unreasonable. [183]

XIV. RESPONDENT'S DISCLOSURE OF REPORTS UNDER FCRA (PARAGRAPHS 22–23 OF THE COMPLAINT)

A. Training

521. After passage of the FCRA, respondent conducted extensive orientation sessions for its employees to acquaint them with new procedures to be instituted upon the Act's effective date in April 1971.

522. After the Home Office had determined the procedures to be instituted and trained the home office staff, training meetings were held for the Regional Vice Presidents in January 1971 (Jenkins 5656–58; RX 551A–D). Each Regional Vice President then met with the branch managers in his region to train them. Home office personnel attended these meetings (Jenkins 5659–60).

523. Branch office managers subsequently conducted training sessions with the personnel in each branch (Jenkins 5660). Follow-up educational branch meetings were held in April 1971 (Jenkins 5680–81; RX 558A–K). Extensive instructional material was disseminated to the branch office managers to aid them in understanding and teaching the new procedures (Jenkins 5660–61, 5669–70, 5675–78; RX 556B–LL, 564A–YY, 120A–Z102). Additional material was sent to branch managers subsequently to direct them regarding modifications and revisions in respondent's procedures related to FCRA (Jenkins 5669, 5678).

524. A home office staff group—the FCRA unit—was established to provide expertise on FCRA problems. Telephones were manned by this team to handle questions from field personnel when FCRA problems arose (Jenkins 5692–93). [184]

B. Disclosure in Branch Offices

525. In April 1971, branch managers were instructed to "choose those Field Representatives you feel are in the best position to handle Inquiring Consumers" and train them to make consumer disclosures (RX 558C). The importance of having "trained personnel" conduct disclosures was stressed, and the branch offices were provided with training materials (including specimen reports with instructions on how they should be disclosed) to be reviewed by the selected personnel as part of their training (Jenkins 5666–68; RX 556N–Z). Respondent continued to emphasize to branch managers that consumer inquiries "require the best ability in the office." (RX 107Z–187).

526. Respondent's instructions stated that when a consumer visited the office for disclosure regarding a report or investigation on him, he was to be given a brochure explaining the disclosure procedure (RX 547B–E, 303A–F; J. Curtis 7192). A consumer contacting an office in connection with disclosure was to receive disclosure of all reports in his file (other than those respondent felt were not covered by the Act) (RX 556DD). In addition, branch managers were instructed that there should be " 'trained personnel' in the *office at all times*" to give disclosure. "It is *not* satisfactory to refuse to discuss a situation or ask the consumer to come back when the Manager returns, except under the most extreme circumstances." (RX 564T, emphasis in original).

527. Respondent's policy regarding charges for disclosure and reinvestigation paralleled Section 612 of FCRA, with no charge authorized for disclosure if the consumer had, within 30 days, received notice of adverse action in connection with a report filed by Retail Credit (RX 120Z–50). In other instances, where the Act permitted charges, respondent's instructions provided for a $5.00 disclosure fee and a reasonable fee for reinvestigation (both fees to be refunded if, upon reinvestigation, the original report information were disproved or not verified) (RX 120Z–51). However, respondent's instructions gave discretion as to whether these charges were imposed at all and gave particular instances in which it was suggested that they not be made (RX 120Z–51–52). [185]

528. Contact by inquiring consumers was to be noted on a monthly log maintained by the branch office (CX 1473). In addition, a file memorandum was to be prepared after the disclosure. This document was to set forth a brief description of the consumer contact and information disclosed (RX 556M; Jenkins 5771–72, Jegley 7038).

Copies of the memoranda were sent to the home office (Jenkins 5771–72).

529. Respondent's instructions, however, were not followed in all instances. Consumer Phares visited Retail's Pittsburgh office in 1972, stated to the receptionist his request "to see someone in regards to information on file." He was told that the information "was not given out" (Tr. 773, 783). Only after Mr. Phares had his attorney call the Retail branch office did he receive disclosure (Tr. 774–76).[191]

530. Consumer Humble visited Retail's Lincoln, Nebraska office in February 1973, after she received a notice from her automobile insurance company rejecting an amendment to her policy to add her husband as an insured (Tr. 3479–82). She was told that the file information was "on" her husband and would not be disclosed to her (Tr. 3484–85). She received no disclosure even though the report was in her name and contained information on her, as well as on her husband (CX 133A–B).[192] [186]

531. Consumer Baker, after having been incorrectly advised by the Wichita branch's assistant manager as to his rights to disclosure (Finding 537, *infra*), took with him to his disclosure appointment Mr. Dickey, a representative of the Consumer Division of his state's Attorney General's Office (Tr. 3113–14). After Mr. Baker indicated that he did not intend to sign a waiver form (CX 337) presented to him (Tr. 3115, 3119), Mr. Smith, the branch manager,[193] inquired regarding Mr. Dickey's identity. After learning Mr. Dickey's identity, Mr. Smith stated, "I'll tell you this much. If I read this report to Mr. Baker, you are not going to be present when it's read." (Tr. 3119). Mr. Dickey advised Mr. Smith of Mr. Baker's right under the FCRA to have a third person present during disclosure, at which point Mr. Smith terminated the interview without making any disclosure (Tr. 3119–20).

532. In 1972, after learning that his daughter had been visited and questioned regarding his wife, consumer McCune called the Wichita branch office to ascertain whether the interviewer was a Retail employee and if a report was being prepared (Tr. 4361–63). The assistant branch manager told him that he had no record of an

[191] In rebuttal of consumer Phares' testimony that he was told his file information could not be revealed, Mr. Peck, the branch manager, testified with regard to the usual procedure when a consumer visited the office for disclosure (Tr. 8360–67). This testimony did not discredit Mr. Phares' testimony based on his clear recollection of what took place at the particular event in question. In addition, the unrebutted fact that Mr. Phares contacted his attorney regarding Retail tends to corroborate his testimony that he had been rebuffed by Retail when he first attempted to obtain disclosure.

[192] Respondent's instructions provided that if information on one spouse was sensitive and likely to be unknown to the other, the discloser might wish to talk with the parties separately regarding information in the file on them as individuals (RX 564V).

[193] CX 1492 indicates that Mr. Smith was the manager of the Wichita branch.

investigation being conducted on the McCunes (Tr. 4363). Mrs. McCune also called Retail and spoke to the branch manager, who told her they had nothing in their files (Tr. 4384). When the McCunes received a notification that Mrs. McCune's insurance application had been denied on the basis of a Retail Credit report, it became apparent that a Retail report had been prepared (Tr. 4363–64). Mr. McCune again contacted Retail and after asking the branch manager where the information was obtained, was told that all Retail's information was confidential and that "they couldn't tell me a thing, and at that time they didn't tell me whether they even had any record of it." (Tr. 4365). Only after Mr. McCune became aware of the right to disclosure and so informed the branch manager, was he told disclosure could be obtained (Tr. 4366). [187]

533. Respondent violated Section 609 of FCRA by denying disclosure to consumers (Findings 529–32). In addition, the failure of Retail to advise the McCunes upon their first contacts that a report was being prepared or an investigation conducted, discouraged disclosure in a manner tantamount to refusal to disclose (Finding 532).

534. In other instances, respondent's field personnel, while not actually refusing disclosure, imposed certain conditions on or prerequisites to disclosure, which were not permitted by FCRA.

535. It was respondent's practice to request that a consumer seeking disclosure sign a completed Consumer Interview Form (RX 556L). This form had blanks for the consumer's name, address and other identifying information, and for the signature of the consumer to certify that he was who he purported to be (CX 1457). Respondent's stated purpose of this procedure was to provide information adequate to ascertain that disclosure was being made to the proper person (McLaughlin 8346; Dukes 12735, 12741; Jenkins 5689–90; see also CX 675Z–62–63). However, the form, above the signature line, contained the following paragraph:

> I hereby certify that I am the above described consumer and request that Retail Credit Company disclose to me the nature and substance of information which it has in its file concerning me. I authorize Retail Credit Company to make necessary investigation of any item which I may dispute and to transmit the results of such investigation to any person to whom it has previously reported such disputed information. I authorize any business, organization, professional person or anyone else to give full information and records about me.

(CX 1457, CX 337.) [188]

Thus, as noted by respondent, the form "when properly signed"

could serve as an authorization for ascertaining medical information (RX 108E).[194]

536. Such a waiver was not necessary for identification purposes and was not a proper condition to place on disclosure. Respondent did not impose the condition of this waiver on all disclosures (*e.g.*, telephone disclosure, when given, did not involve the waiver), and did make disclosures when confronted with consumers who refused to sign the waiver (Luster 3172–73, 3180; Bendelow 3459–62). However, its use of the form implied a condition to persons unaware of their right to disclosure without signing a waiver.[195]

537. Another condition imposed on disclosure occurred in the case of consumer Baker. Mr. Baker requested disclosure in 1973, after receiving a cancellation of his automobile insurance (Tr. 3108–10). The assistant manager told him there would be a $5.00 charge for disclosure. Mr. Baker stated that he would not pay a $5.00 fee and showed the assistant manager his cancellation notice (Tr. 3110[196]). The assistant manager then told him, contrary to any corporate policy or instruction, that he would have to have a written authorization from the insurance company involved before he could receive disclosure (Tr. 3110–11). After learning of his rights under FCRA, Mr. Baker again contacted the assistant manager who insisted that a written authorization was prerequisite to disclosure (Tr. 3112–13). Mr. Baker then returned to the branch [139]office with a state consumer representative, well versed on the FCRA. At this meeting, the branch manager gave him the Consumer Interview form to sign for disclosure and the insurance company authorization was not demanded (Tr. 3114–15).[197]

538. Respondent imposed conditions on consumer disclosure which were not authorized by the FCRA (Findings 535–37). Imposition of such conditions is another way to avoid the disclosures required by Section 609 of FCRA and is constructive refusal to give disclosure. Such practices violate Section 609 of the Act.

539. Respondent's instructions stated that disclosure of the nature and substance of the information in the file was to be given, "not necessarily verbatim" (RX 556L). Under no circumstances was the discloser to permit the consumer to see, read or handle the report

[194] In 1974 or 1975, respondent redesigned its Consumer Interview Form and omitted the waiver clause (McLaughlin 8347–48; RX 492C).

[195] The field personnel were instructed that if the consumer refused to sign the form, they were to ask for other identification and not to insist that the consumer sign the form (RX 556I).

[196] No finding of violation is based on the attempted imposition of a fee. Mr. Baker's testimony indicates that when the assistant manager mentioned the fee, he had not been advised that Mr. Baker sought disclosure because of an insurance denial (Tr. 3110).

[197] Disclosure in this case did not occur. After the branch manager learned the state representative's identity and that Mr. Baker intended he be present throughout the interview, he terminated the meeting (Finding 531).

himself (RX 556F, 556L). "Nature and substance" was defined to include "*ALL* file information," favorable and unfavorable. Summarizing and paraphrasing were permitted "so long as we are complete, accurate, and the consumer understands." (RX 564W, emphasis in original). The instructions further provided that, in disclosing a report, the discloser cover all the questions and answers on the report and then take the narrative sections "feature by feature." (RX 564X).[198] [190]

540. "As a matter of established procedure or usual and customary practice, respondent [did] not disclose the recipient of a consumer report on the consumer which it [had] furnished for employment purposes within the two-year period preceding the request, or, for any other purpose within the six-month period preceding the request, unless specifically requested to do so by the consumer." (CX 1445E). Likewise, respondent did not disclose non-investigative sources of information without a specific request (RPF 935).

541. Implementation of respondent's instructions in the field was not uniform. In some branch offices, reports were read verbatim (Burge 5088–89, Jegley 7027). In others, a summary or paraphrase of the report was disclosed (Coulter 8202–03). In still another, only the part of the report which the discloser "assumed was the factor" that had caused the consumer to be rated or denied insurance (Hakey 1664–65) was disclosed.

542. In practice, some field personnel, while purporting to give the nature and substance of reports, failed to give adequate or complete disclosure.

543. In November 1971, a consumer went to the Wichita branch office for disclosure to ascertain what information had been the basis for denial of two insurance applications (Tr. 3377–81). He received disclosure and was told that his life insurance was probably denied because he had had pneumonia and that the basis for his automobile cancellation was probably his six traffic violations in 6 years (Tr. 3383–89). When the consumer asked for the exact reasons he had

[198] Ex-employee Shelley testified at length regarding instructions he allegedly was given by Mr. Browning, the Regional Vice President in Mr. Shelley's area. These alleged instructions were contrary to respondent's written instructions, *e.g.*, in making disclosures, personnel should tone down the reports (Tr. 15115), not disclose the question and answer portions of the reports (Tr. 15116), "highlight" the body of the report (Tr. 15116–17), and if a report contained several adverse items, disclose the item of "least conflict" first because the discloser would often "not have to go the remainder of the report." (Tr. 15117). Mr. Browning specifically denied giving these instructions (Tr. 16098–104). His denial was supported by other Retail employees in Mr. Browning's area who testified regarding instructions he had given them which were inconsistent with those Mr. Shelley allegedly received (Lindsey 16182–85, Beckman 16312, Taylor 16218, Klueh 16274–76). After considering this testimony and the fact that it is highly unlikely that a vice president would issue directives so widely divergent from the instructions he was given by the Home Office (which he knew were given to the branch offices by the Home Office), it is found that Mr. Shelley's testimony was effectively rebutted on this critical issue. His testimony is, therefore, not relied on.

been refused, he was referred to the insurance companies (Tr. 3389). He contacted the insurance companies and was told he would have to receive the information from Retail (Tr. 3390–91). The consumer returned to Retail and had a second disclosure similar to the first (Tr. 3391–92). He again contacted one of the insurance companies about his refusal. The insurance representative finally told him that the Retail report indicated that he had a drinking problem (Tr. 3392–93). Since no information regarding drinking had been disclosed to him by Retail, he returned for a third disclosure, in which the drinking information was again not mentioned (Tr. 3393–94). The consumer asked about any drinking information, and the branch manager stated, " 'I didn't feel that it was important' " (Tr. 3394).[199] Among other items not disclosed to the consumer were that he was "said to be a fast and careless driver;"[200] that he was "said to be an unstable type of person, not regarded well;" that his mother had been in a mental institution and was poorly regarded, and that he had a girlfriend who drove his car (Tr. 3397–3401, 3384–85; CX 343H–I). **[192]**

544. Consumer Grabher contacted the Denver branch office after she received an insurance cancellation (Tr. 3410). She received disclosure but was not told the report's statement of her estimated income and net worth (Tr. 3412–13; CX 113A).[201]

545. In 1972, two consumers, father and son, visited the Dayton branch office for disclosure after an insurance company had refused the addition of the son to the father's automobile insurance policy (Tr. 960–62). Information suggesting the son had been involved with drugs and unfavorable details of his having been terminated from a teaching position were not revealed (Tr. 964, 967). The remaining information, which was disclosed, was basically favorable (Tr. 978, 982–84). Afterwards, the father wrote the insurance company involved, asking whether the denial was based on additional information since the Retail report was favorable. The son thereafter received a telephone call from the Dayton branch manager, who stated that the employee who had conducted the disclosure, had overlooked one page of the report. He then disclosed to the son the

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[199] The information which the Retail representative did not consider important was: the consumer had been seen "drunk several times since he was discharged from the military. One source stated that prior to service, the subject was arrested for driving his car with some of the tires on the sidewalk down the middle of the town." (CX 343I).

[200] This item appears to have been disclosed in the second disclosure session (Tr. 3400).

[201] Ms. Grabher's testimony was more persuasive than that of the rebuttal witness who testified regarding the disclosure procedure he generally followed.

drug information and unfavorable details of his dismissal from the teaching position(Tr. 965–67, 979–81; CX 98).[202] [193]

546. Consumer Smith twice received disclosure in 1973 from the Manchester branch office of a report which was the basis of his failure to receive an insurance agency appointment (Tr. 927–32; CX 258). These disclosures did not include unfavorable information in the report concerning previous employment (Tr. 930–32). While the information in question was later deleted from the report and a notice of the deletion sent to the company who had received the report (CX 255A–C, 257; Tr. 952–53, 8461–62), this action was taken without Mr. Smith's knowing the information was in the report.[203] [194]

547. Another consumer received disclosure in 1972 from the Oxon Hill, Maryland office after she received an insurance cancellation (Tr. 1792–94). Items from a report dated December 15, 1971 (CX 151) were revealed, but the disclosure did not include information in another report, dated December 27, 1971 (CX 152), that the consumer had run off with a truck driver; that her morals were questioned; and that she was regarded as "trying to take [her husband] for his money." (Tr. 1794–96; CX 151A–B, 152A–B).[204]

548. Consumer Dayton contacted Retail's Phoenix office in 1973, after her automobile insurance was cancelled (Tr. 3531–32; CX 1469B). She received disclosure of some information, including information that she was living with a man to whom she was not married (Tr. 3533–34). She was not told, however, that the man living with her had caused trouble in the neighborhood (Tr. 3534). Also, her estimated income and worth were not revealed (Tr. 3534–

[202] The son's testimony that, following his disclosure, he received a call from Retail and was told that during the disclosure, one page of the file had not been disclosed to him, was unrebutted. This fact, together with the branch manager's testimony that the employee who made the disclosure "was not sure" he had disclosed the items in question (Tr. 14899), gives credence to the consumers' testimony, despite the testimony of rebuttal witnesses.

[203] Consumer Smith's testimony that unfavorable employment information was not disclosed to him is found credible, despite rebuttal testimony of the Retail employee who gave the disclosure. The rebuttal witness testified that the items were disclosed and disputed (Tr. 10890), and that a reinvestigation was conducted (Tr. 10891–92, 10897). However, Mr. Smith appeared to have a clear recollection of what was disclosed to him. His recollection was particularly convincing because he had discussed with Retail in 1968, the subject information and was under the impression the material had, at that time, been deleted from his records (Tr. 918–27). That Mr. Smith would have remembered if this information was mentioned seems certain. Furthermore, the visit of Mr. Yox, the branch manager, to Mr. Smith's office to give another disclosure (Tr. 942–45, 8457–60) tends to corroborate Mr. Smith's testimony that the first disclosures were incomplete. During disclosure by Yox, the then-deleted information was disclosed to Mr. Smith. Mr. Yox told Mr. Smith that the information had been included in the report because the wrong report had been sent to the customer and that during the previous disclosures, the wrong report was read (Tr. 945–46).

[204] Respondent's suggestion that there need be evidence that the second report, a prior address report, was actually in respondent's file at the time the consumer received disclosure, is without merit (RPF 817). Respondent had a duty to give disclosure of all reports in a consumer's file. When all reports were not disclosed, it was incumbent upon respondent to show that the reports not disclosed were not in the file. Here, no such showing was attempted.

35; CX 78A–B). Ms. Dayton would have disputed these items if they had been disclosed (Tr. 3534–35).[205]

549. In 1972, a consumer was given disclosure by Retail's San Francisco office of reports prepared in connection with his application for life insurance made at the request of the bank from which he and his partner in business had a loan (Tr. 3711–13, 3725). [195]One item was withheld. He was not told that his file contained a statement that he used "his hands in an effeminate manner, also talks in an effeminate manner." (Tr. 3720; CX 218).[206]

550. When consumer Phares (Finding 529) received disclosure of his report, he asked what companies had recently received the information disclosed. He was told this information would not be divulged (Tr. 777, 787–88).[207]

551. In other instances, while not completely omitting items from the reports, Retail representatives "paraphrased" or "summarized" the items in such a way that the full meaning, and in some cases, the derogatory tone of the report, was not conveyed to the consumer.

552. Another consumer contacted Retail's Canton, Ohio office in 1972, and asked why her policy had been cancelled. She was told that her report indicated she had an unstable marriage (Tr. 3593–94). The report actually stated she had been separated several times from her husband and that two sources "indicated that [her husband] had a desire for other women and they also stated that . . . your insured had a desire for other men and between the two this caused friction in the marriage. Stated were fighting constantly." (CX 169B).[208] [196]

553. Another consumer was told that her report indicated she "had recently had a run-in with [her] former husband, a severe one." (Tr. 1794). The report actually stated that she had been assaulted by her husband and incurred 22 stab wounds as a result (CX 151A).

554. When consumer Stanley received disclosure from the Wilmington, North Carolina branch office after having his insurance cancelled (Tr. 220–26), the file information was presented in a far less inflammatory manner than in the report. *E.g.,* Mr. Stanley was told the report indicated he made it a point to be well aware of the

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[205] Ms. Dayton's testimony was more convincing than that of the rebuttal witness who testified regarding only the usual procedures followed.

[206] The consumer's testimony was not rebutted. It is respondent's position that disclosure to the consumer was not required under FCRA because the report prepared was not a consumer report (RPF 818). However, Section 609 of FCRA requires disclosure of all file information on a consumer (except medical information), not just consumer reports (see Finding 559, *infra,* pertaining to claim files).

[207] Mr. Phares' testimony that he was told the recent recipients of his report would not be divulged to him was unrebutted. Confusion in peripheral areas of his testimony does not detract from the weight to be given to this unrebutted testimony.

[208] This consumer's disclosure was also incomplete in that she was told information only in response to specific questions she asked. After being told the reason for the cancellation, she asked whether the report showed she was married, and where it indicated she worked (Tr 3594). She was given this information, but only after she asked specifically (Tr. 3594–95). No witness was called to rebut the witness' testimony.

benefits to which he was entitled under insurance policies (Coulter 8198–99), whereas the report actually stated:

. . . Special attention has been given to past losses due to subject being well-known in this area, as being extremely "claim conscious" and has submitted several minor claims with several different insurance companies. We did develop through outside sources that the subject has had his insurance cancelled on several occasions due to excessive claims. Subject is known to be the type person that will submit any claim and usually has a full knowledge of what is covered and what is not. This information was verified through outside sources as well as the local claims adjuster who has worked with the subject in settling several claims.
(CX 271A–B.)

In addition, the report stated:

. . . The subject himself is favorably regarded but his general financial reputation is not good, sources report that he has the ability to pay but general nature is to be slow making payments. We developed a past-due account with the local hardware store over two years past-due and also a past-due account with a local carpet-laying firm over a year past-due with no attempt made to pay.
(CX 271B.) [197]

On this subject, Mr. Stanley was told only of the specific past due accounts and that his reputation for bill paying suffered because of them (Coulter 8200–01).[209]

555. Respondent's field personnel failed to give the nature and substance of the information in its files in a substantial number of disclosures, by either omitting pertinent information or summarizing and paraphrasing to the extent that the information disclosed did not reflect the full import of the information in the reports (Findings 543–54).

556. In June 1974, respondent instituted "visual disclosure" for consumers visiting an office for disclosure (RX 576A–E). This procedure was developed because "it became apparent over the years that no matter whether or not our manager, or when our manager read a case verbatim across the desk, some of our consumers did not feel that he was doing so." (Jenkins 5763–94). Under the new procedure, the consumer could actually see his report and review it with the Retail representative.

557. In 1976, Retail again revised its disclosure procedure. As of October 1, 1976, a consumer who visits the office for disclosure is to be given a copy of his report after visual disclosure is given (or in the case of telephone disclosure, on a subsequent visit to the office) (RX 122A, C–E).

[209] Mr. Coulter, who made the disclosure, testified in connection with Mr. Stanley. Mr. Coulter's statements themselves form the basis of this finding.

C. Disclosure of Claim Reports

558. It is respondent's position that claim reports are not consumer reports under the Act and therefore not subject to its disclosure requirements. However, on some occasions, in order to accommodate consumers, claim [198]reports have been disclosed." (RPF 810(a)).[210] This policy was communicated to the field. As one of respondent's officials explained, he felt no "corporate obligation" to disclose claim reports. "The company policy was that claims versions were not part of the Fair Credit Reporting Act but on each and everyone you had to handle it individually on how you saw—how—if you wanted to disclose part of it. If you saw it feasible to do so then you could do so but it is a matter of convenience to the consumer more so than company policy in that particular aspect." (Piercey 8323).

559. Respondent's position that claim reports need not be disclosed and the ad hoc position with respect to disclosure taken in the field[211] compels the inference that many claim reports were not disclosed. Such failure to disclose claim reports violated Section 609 of FCRA requiring disclosure as to "all information (except medical information)" on the consumer in the files of a consumer reporting agency at the time of the request. [199]

XV. TELEPHONE AND SUBOFFICE DISCLOSURE (PARAGRAPHS 24-25 OF THE COMPLAINT)

A. Telephone Disclosure

560. Respondent's instructions regarding telephone disclosure stated that even though the FCRA authorized Retail to require a written request prior to telephone disclosure, no such requirement was imposed by the Company (Burge 5006-07). Rather, the Retail representative was required to make certain he was speaking with the proper person (CX 675W). Telephone disclosure was encouraged, at least indirectly, by respondent's statement to branch management that as many routine situations as possible should be handled by

[210] The record indicates that, as of June 18, 1971, respondent did recognize that Section 609 covered not solely consumer reports, but "all of the information about the consumer" (except medical information) in the files (CX 675Z-21). However, to the extent of any conflict between this document and respondent's proposed finding, respondent's finding is relied on as to the procedure actually followed.

[211] *E.g.*, when consumer McCreary requested disclosure of his claim report from the Miami branch office, he received disclosure only of the portion of the report called the "claimant interview" rather than of the entire report which included information from other sources (Tr. 8317; RX 449B-C). Consumer Beresh received disclosure of claim information a week after he originally requested it (Tr. 11094). The disclosure occurred only after Mr. Beresh called the branch office numerous times and Retail's legal department (whom the branch manager had contacted since he felt claim reports were not covered by FCRA), told the branch manager to "go ahead and disclose" (Worman 11086-87, 11092-94).

telephone (RX 564S). In addition, branch managers were urged to "make every effort to make good" with a consumer on the first contact and told that "delay irritates." (RX 107Z–187).

561. Field personnel were instructed that if a consumer telephoned for disclosure, properly identified himself and the pertinent file contained no protective or decline information that was subjective or highly critical, the written request was to be waived (CX 675Z–31). Otherwise, the branch management was to suggest the consumer come by the office for disclosure or send a written request for telephone disclosure (CX 675Z–32). If a consumer wrote to Retail requesting disclosure, he was to be advised by mail that he could telephone for disclosure, but if the report was highly sensitive, it was suggested that the letter "be pitched toward a private, face-to-face disclosure" (CX 675T). It was felt by respondent that while telephone disclosure saved time for all parties involved and even sensitive material could be handled by telephone, there was "no substitute for a face-to-face discussion"(RX 108B). Similarly, Mr. Hakey testified that if the information in a consumer's file were not "minor," he wanted the person to visit the office to ascertain identity (Tr. 1661–62).

562. Respondent's instructions regarding telephone disclosure were not followed in all the branch offices. [200]

563. It was the policy in the Denver branch office for the receptionist, Ms. Dukes,[212] to advise consumers who telephoned in for disclosure that the information requested was confidential and could not be disclosed by telephone. Callers were advised of their right under FCRA to in-person disclosure, but no mention was made of their right to telephone disclosure if a written request were filed. On the "rare" occasion when a consumer stated he was unable to come to the office, Ms. Dukes referred the call to the branch manager or assistant manager (Tr. 12739). Ms. Dukes received her instructions on what to say to consumers from the branch manager (Tr. 12740, 12739, 12741).[213] Consumers Bendelow (Tr. 3452–53), Coons (Tr. 3578), Comerata (Tr. 3218), Goddard (Tr. 3156–57), Moser (Tr. 3561–62) and Van Sickle (Tr. 3823–24) were refused telephone disclosure by the Denver office through implementation of this policy. Consumer Grabher, who asked to and did speak with the manager when she called, was asked by him to come in person in order to obtain

[212] Ms. Dukes was receptionist in the Denver office from 1970 until January 1976 (Tr. 12733, 12738).

[213] Mr. Hendon, the branch manager, testified and did not directly dispute Ms. Dukes' testimony regarding her instructions or the procedure she described. He testified that telephone disclosure was given by the Denver office when a consumer sent a written request (Tr. 11899–900) and that, on occasion, when he felt identification had been properly demonstrated, he gave disclosure when there was no written request (Tr. 11900). In addition, RX 519, 520A–B, 521, 522, 524, 525A–C, 526A–B, 530–543 indicate that some telephone disclosures were made by the Denver office.

disclosure. Only after telling the manager she was at work, could not come in and wanted to know immediately why her insurance was cancelled, was she given disclosure by telephone from the Denver office (Tr. 3410–11). [201]

564. The manager of the Wichita branch office told consumer McCune that the only way disclosure could be given was in person (C. McCune 4366). Consumer Mumford was told by respondent's Rocky Mount, North Carolina office representative that disclosure could not be given by telephone (Tr. 1146).[214]

565. Respondent has told consumers that disclosure could not be given by telephone without mentioning that, with a written request, consumers have a right to telephone disclosure (Findings 563–64). Thus, as to these consumers, respondent eliminated, as a practical matter, the option for telephone disclosure which the FCRA sets forth and have violated Section 610 of FCRA.

566. In the Brockton, Massachusetts and Lincoln, Nebraska branch offices, respondent advised consumers who contacted Retail requesting copies of their reports that, while no copies could be sent to them, they could receive disclosure of their files at the branch offices [202](Humble 3481–82,[215] Reinhardt; RX 468J; CX 243J[216]). No mention was made of the consumers' rights to have disclosures by telephone.

567. Thus, respondent advised consumers obviously interested in learning what was in their files that disclosure was available in a Retail office without mentioning the possibility of telephone disclosure (Finding 566). Even though telephone disclosure was not specifically requested in these instances, respondent, by undertaking to advise consumers of their rights regarding disclosure and only partially advising them as to their rights has, in a practical sense, made telephone disclosure unavailable to them in violation of Section 610 of FCRA.

B. Suboffice Disclosure

[214] While Mr. Mumford's testimony on the actual disclosure given him and the subsequent reinvestigation was too confused to ascertain precisely what disclosure was given, his unrebutted testimony was clear that he called the Rocky Mount office and was told that disclosure could not be given by telephone. As respondent pointed out (RPF 949f), Mr. Mumford was told that the reason telephone disclosure couldn't be given related to inadequate identification by telephone (Tr. 1159–60). Nevertheless, he was apparently not told that he could receive disclosure with proper identification or a written request (see Tr. 1146). Mr. Mumford was given some information from his file by telephone regarding marital discord (Tr. 1146, 1160), but he received no disclosure of the specifics of the report until he later visited the Rocky Mount office (Tr. 1147–50) located 40 miles from his home (Tr. 1145).

[215] Ms. Humble's testimony was not discredited by the rebuttal witnesses' general testimony to the effect that 75 to 85 percent of the disclosures from that office were by telephone (Tr. 8345).

[216] In the case of consumer Reinhardt, it should be noted that the response she received from Retail was less informative than that given by Retail to a friend of hers in response to a similar request. Her friend had indicated in his request for a copy of his report, that he had some knowledge of the FCRA. (Compare RX 468I and CX 244 with RX 468J and CX 243).

568. When respondent established its disclosure procedures after passage of FCRA, a corporate policy decision was made that there would be no "systematic disclosure" from the suboffices because the suboffices were not adequately staffed for this function (Burge 5008–09).[217] [203]

569. A suboffice is generally removed from the metropolitan area, located in a small city or town (Case 5362). It is staffed by one or more field representatives, and, in the case of those having more than one field representative, one of them is designated as the supervisor. There may or may not be part-time or full-time clerical personnel (*e.g.*, Jegley 7057–58). In some cases, the suboffice is located in the field representative's home, and the Company pays him for his telephone expense and rent on the space used (Brothers 7358). The number of suboffices also varies from time to time (R. Jones 5218). No files are maintained in suboffices (Burge 5010).

570. The suboffice personnel were instructed that when they were visited by inquiring consumers, they were to secure information on consumer forms and advise the consumers that either the branch manager or the suboffice representative would be in touch with them (RX 564T).

571. After a consumer's visit to a suboffice, a memorandum relating the contact and information obtained was to be sent to the branch manager for his handling (RX 564T). Some suboffice disclosure was apparently anticipated as instructions stated that the branch manager would decide whether to contact the consumer or send the consumer's file to the suboffice with instructions regarding disclosure to the suboffice personnel (RX 564U; CX 675Z–64). If a consumer telephoned a suboffice for disclosure, the Retail employee was to suggest he phone or write the branch office manager and to supply information facilitating such contact (CX 675Z–63, 64). The branch office manager had discretion regarding whether to have disclosures given in the suboffices (Jenkins 5771).

572. In accordance with this policy, respondent admitted that, on occasion, it did not make disclosures at suboffices (Answer, Par. 24).[218] [204]

573. Respondent's failure to provide disclosure at suboffices does not violate Section 610 of FCRA.

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[217] The reason for this decision was stated to be that "there is not personnel present in the sub-office, certainly not in the smaller sub-offices, at all times or even in the working hours, because they may well be gone from the office during the working hours. More likely, they would be there in off-hours rather than in working hours. So we decided at the outset we would not disclose in sub-office points." (Burge 5009).

[218] When consumer Roberts requested disclosure from the Idaho Falls suboffice, he was referred to the Boise branch office (Tr. 3358–61, 12661–62).

XVI. REINVESTIGATIONS (PARAGRAPHS 26-27 OF THE COMPLAINT)

574. Field management was instructed that during disclosure, the Retail representative was to note the items the consumer disputed (RX 556L). If the dispute was of a minor point, such as a street address, exact amount of income, dates, or numbers of children, and the item had "no adverse effect on the transaction," the report was to be corrected accordingly, and if the consumer requested, a copy of the correction was to be sent to the recipient company (RX 556F-G). In all other cases of dispute, the Retail representative was to take down the "consumer's side of the situation" on a Consumer's Statement form (CX 675Z-22), and there was to be a reinvestigation (CX 675X). If the consumer disputed information in his file but stated that he did not want a reinvestigation, he was to be told that the law required there be a reinvestigation. If he remained adamant in his position, the Retail representative was to get a written statement of his dispute and a written statement from the consumer that he requested there be no reinvestigation (CX 675Z-36).

575. When a reinvestigation was conducted and the original report information confirmed, the Consumer's Statement was to be sent to the recipient company upon the consumer's request (and the Retail representative was required to advise the consumer of his right to so request). The Consumer's Statement was made a part of the consumer's file (RX 556M).

576. If the reinvestigation did not verify the original report, the information was to be deleted or corrected, and the amendments sent to the recipient company. This procedure was not to be followed, however, if respondent felt that the consumer had exerted pressure on sources and, as a result, they would no longer discuss the matter with Retail, thus precluding verification. [205]In that case, the customer would be advised of the dispute, the circumstances of why the information could not be verified, and a copy of the Consumer's Statement would be sent to the consumer (RX 564EE).

577. These explicit instructions, when implemented by respondent's field personnel, resulted in situations where no reinvestigations were conducted though consumers clearly disputed information given them during disclosure.

578. One consumer received disclosure from the Baltimore branch office in 1972, after she was denied automobile insurance (Tr. 1496). She disputed much of the information contained in the report, *e.g.*, that her house had constant traffic of people and was thought to be a "house of ill repute;" and that her babysitter had taken drugs as

a result of the consumer's influence (CX 280B; Tr. 1530). The consumer's statements of dispute were recorded in a memorandum prepared by Retail after the disclosure (RX 477A–B), and she was told there would be a reinvestigation (Tr. 1505–06). There is no evidence in the record that a reinvestigation was conducted or that the insurance company involved was ever notified that the consumer disputed anything in the report. The fact that the consumer was invited by the insurance company some 3 years later to reapply for insurance is not relevant.[219]

579. Another consumer visited the Boise office and received disclosure of a report prepared on him which was the basis of a health insurance denial (Tr. 4284–87). The report contained many items of an adverse nature, *e.g.,* that his restaurant was closed because he put dog food in his tacos; that he and his wife were arrested in a drug raid and "continued to have illegal drug habits;" that he had been charged with several other crimes; and that he grew marijuana in his backyard [206](CX 1484A–B). During and after the disclosure, the consumer indicated that the report was inaccurate (Tr. 4289–96). He was told that he could dispute specific items and that a reinvestigation of the information he disputed would be conducted (Tr. 4296). While he declined to go over the report stating exactly which items were inaccurate, he stated that everything below his name and address was incorrect (Tr. 4296), and made it known that he strongly disagreed with the report.[220] At one point, he suggested that the discloser ascertain that his restaurant had never been closed on a dog food charge by simply calling the county health department (Tr. 4316–17). In addition, the consumer mentioned suing Retail (Tr. 4310). The next day, the consumer brought his lawyer with him to Retail, received another disclosure (Tr. 4287, 4312) and was again told he could have a reinvestigation conducted if he would specify the items with which he disagreed (Tr. 4313–15). The consumer later wrote a letter to Retail requesting a copy of his report (CX 1485). He received a letter in reply, stating that a copy could not be sent but a reinvestigation would be conducted "[i]f you consider any of the information which has been disclosed to you to be incorrect." (CX 1486). The consumer did not respond to the letter, but turned the matter over to his lawyer (Tr. 4298–99). Mr. Miley, who gave the disclosure, did not order a

[219] The branch manager of the Baltimore branch office testified in rebuttal to this consumer. However, he did not dispute the evidence relied on in this finding regarding reinvestigation.

[220] Typical of the consumer's statements of dispute during the disclosure were: "I told him it was incorrect" (Tr. 4289); "I told him it was completely wrong" (Tr. 4290); "I told him it was a blatant lie" (Tr. 4291); "I said again those were blatant lies" (Tr. 4293); "I told him it was the most ridiculous thing I had ever heard of" (Tr. 4294). While the discloser stated that Retail would reinvestigate if the consumer would state specifically what he objected to, the consumer felt "he wasn't listening to what I was saying. If I call something a lie, I'm disputing it" (Tr. 4314).

reinvestigation (Tr. 11142). It was his practice that when a consumer simply stated an item was inaccurate and refused to go further, he did not order a reinvestigation (Tr. 11143). Mr. Miley referred the matter to [207]respondent's legal department (RX 807C–D) in compliance with respondent's instructions to do so when a consumer threatened suit (Tr. 11142). Failure to order a reinvestigation after the consumer disputed information in his report violated Section 611 of the Act.[221]

580. After consumer Kasdorf received disclosure from the Albuquerque branch office, a consumer statement was written showing that he disputed certain items disclosed to him: that he was a slow payer of bills and had left a former residence owing rent (Tr. 12254–55; CX 138A; RX 440E). Mr. Kasdorf assumed the information would be corrected (Tr. 3144). No reinvestigation was conducted (Tr. 11860–62), and there is no evidence that the consumer's statement was sent to the requesting company.

581. Consumer Wisniewski received disclosure from the Cleveland branch office of information in his report prepared for an automobile insurer that he made fast stops and starts, peeled rubber on his tires, and, therefore, his driving reputation was poor (Tr. 1454; CX 332A–C). Mr. Wisniewski denied that he "peeled rubber," although he explained that fast stops were appropriate in some circumstances (Tr. 1454, 1459–60). He filled out a consumer statement denying the peeling of rubber and the fast stops and starts (RX 494C). He provided the names of three people who he said could speak regarding his driving. No reinvestigation was conducted. Retail advised the insurance company involved that Mr. Wisniewski had received disclosure, [208]had "admitted that our report was correct," but had stated that the information regarding his driving did not constitute bad driving (CX 334).[222]

582. After consumer Bitney's automobile insurance was cancelled, she contacted the Seattle office and received disclosure (Tr. 3791). She disputed the accuracy or basis of several adverse items in

[221] The record is ambiguous regarding whether a reinvestigation was later conducted and what it included. Respondent does not allege there was a reinvestigation (RPF 969d), but a letter to the insurance company 2 months after the consumer's visits states there was a reinvestigation and mentions two of the items the consumer disputed (CX 1488). Even if a complete reinvestigation was conducted, it was not timely made and did not cover all the items disputed or adequately set forth the extent of the dispute (see CX 1488).

[222] The discloser, Mr Crawford, testified that the consumer statement and names of references were submitted at a subsequent visit of Mr. Wisniewski after he had consulted with his insurance agent (Tr. 9534). Even if this fact is true, respondent failed to adequately advise the insurance company of Mr. Wisniewski's initial dispute of the peeling rubber item and the obvious dispute of a poor driving reputation. The letter to the insurance company states that Mr. Wisniewski agreed with everything in the report (CX 334). While the existence of a dispute may not have been clear at the first meeting, the consumer statement which Mr. Wisniewski later brought to the office and the bringing of references clearly demonstrated that Mr. Wisniewski disputed his report and desired a reinvestigation. Thus, even if a reinvestigation was not clearly called for after the first meeting, the requirement for one was clear after the second meeting.

the report relating to her children's behavior and reputation and to her reputation and supervision of her children (Tr. 3792–96, 3806; CX 41A–B, 42A–B). She was told that nothing could be deleted from the report (Tr. 3796, 3807), but that she could file a statement adding to the information (Tr. 3796, 3807). She indicated that she felt the report contained assumptions with no verification and that she would follow up researching herself things that were mentioned in the report, *e.g.*, the police's having been called to her apartment, and that she would try to get a statement from the manager of the apartment, the scene of many of the adverse items (Tr. 3806–07).[223] She was not told that she could [209]have a reinvestigation (Tr. 3796; RX 404A–B).[224] While Retail advised the insurance company of the disclosure and clarified two points in the report (CX 43), no reinvestigation was conducted and no mention was made in the notice to the insurance company that she disputed many more of the items in the report.

583. After another consumer received an automobile insurance cancellation based on a Retail report, she contacted the Fresno branch office (Tr. 4126–27). She was told that "based on the information that was turned over by the investigator that they wouldn't insure us because my daughter had been involved in a bomb threat and I [had been] in a mental institution for a year." (Tr. 4128). The consumer disputed these two items and requested a reinvestigation (Tr. 4128–29). A reinvestigation was conducted and the item involving the daughter was found to be in error (RX 451H–I). The reinvestigation did not verify that the consumer had been in a mental institution; however, the sources interviewed for the reinvestigation indicated that she may have had some medical problems in the past (RX 451H–I). The summary of the reinvestigation states, "Unable to develop further health history on wife, however, if desired maybe should obtain release to obtain her physician's records." (RX 451I). Retail's handling of the reinvestigation regarding the consumer's health was not adequate. Either the reinvestigation summary should have stated that the information was not confirmed and, therefore, should be deleted or Retail should have attempted to obtain a medical authorization from the consumer to

[223] A letter was later received by Retail from personnel of the apartment (CX 44B).

[224] Mr. Best, the discloser, stated that when a consumer did not really dispute the information, but only added to it, he did not order a reinvestigation (Tr. 11672). While Mr. Best testified that Ms. Bitney did not dispute the information, it is unclear whether he actually refuted Ms. Bitney's recollection of the disclosure or merely had a different definition of "dispute." Mr. Best testified that Ms. Bitney visited Retail after her first disclosure to review the file again and expressed the desire to file a statement. This testimony is consistent with Ms. Bitney's testimony that she disputed the report. Her testimony is given more weight than Mr. Best's memorandum, after Ms. Bitney's first visit, which states that Ms. Bitney indicated that "the report was substantially correct." (RX 404A).

further investigate this matter. Under the circumstances, failure to delete the information violated Section 611 of the Act. [210]

584. Respondent has failed, in certain instances, to provide reinvestigations required by Section 611 of the FCRA when consumers disputed their reports (Findings 578–82). In certain instances, respondent compounded the effects of its failure to reinvestigate by providing notification to the recipient companies which inaccurately or incompletely set forth the disputes by the consumers (Findings 581, 582).

585. When consumer Mattos requested her reinvestigation, she was told by the Fresno office that there was a charge of $5.25 (Tr. 4129, 4132–33). The request for reinvestigation came within 30 days of the Mattoses' receipt of an insurance denial (RPF 971c). Imposing the condition of a charge on reinvestigation could discourage reinvestigation and is an unlawful condition, even though the money Mrs. Mattos paid was later returned to her (Tr. 4129).[225] By imposing a condition on reinvestigation, which was not authorized by the FCRA, respondent violated the Act.

586. In the case of another consumer, Retail prepared a report on her in January of 1973, in connection with automobile insurance (CX 114A–B), in which it stated that she lived with a man. Later in the month, Retail handled a reopen requested by the insurance company regarding this item. As a result of the reopen, Retail advised the insurance company that "We reinvestigated and confirmed that subject is living with this man . . . Information fully confirmed in both investigations." (CX 146). After the consumer's automobile insurance was cancelled, she received disclosure from Retail's Portland office (Tr. 4479–80). At that time, she disputed the fact that she lived with a man and gave the [211]names of several people who knew she was not living with a man (Tr. 4481). Retail reinvestigated this point and interviewed Mrs. Williams, the wife of the assistant manager of the apartments the consumer lived in, who stated that the consumer was not living with a man (Tr. 4497–98). Retail prepared a new report which eliminated the reference to her living with a man and sent it to the insurance company (CX 148A–B). Accompanying the report, however, was a letter to the insurance company which stated:

[The consumer] disputed the fact that she had a man residing with her, admitted to us

[225] See Finding 527 for respondent's policy regarding reinvestigation charges. Apparently, respondent has interpreted the language of Section 612 of FCRA, which specifically authorizes charges for disclosure and notification, as including reinvestigation charges under the same conditions. Such an interpretation has not been challenged in this proceeding and is not here decided, as respondent admits that the charge imposed in the case of Mrs. Mattos was a violation of Company procedure established to ensure compliance with the Act.

that he is a frequent visitor at her home, stays quite late in the evening and on occasion will have breakfast there, arriving sometimes as early as 6 a.m.
We have rehandled this case in its entirety, contacting original and alternate sources, and at this time we are unable to obtain any source who will even admit knowledge of any friends or acquaintances of [the consumer].
Therefore, would you please use the attached report to replace any previous reports on this individual and make any further evaluation of the risk you feel necessary.
(CX 147.)

No mention was made of Mrs. Williams' statement. By sending this letter with the notice of deletion, respondent effectively negated the deletion, particularly in light of the fact that a confirmation had recently been sent to the company on the item in question. In so doing, respondent constructively failed to delete the item in question and violated Section 611 of FCRA, which requires deletion of items which are not verified on reinvestigation.[226] [212]

587. Respondent has failed to delete information that was disputed by consumers and which was not verified on reinvestigation (Findings 583, 586).

XVII. INTERCHANGE OF INFORMATION BETWEEN CLAIM AND CONSUMER REPORTS (PARAGRAPHS 28–29 OF THE COMPLAINT)

588. Prior to May 1974, respondent's claim reports were filed in the same reference files as its underwriting reports (Burge 5041, Jenkins 5798). When an investigator received a request for a current report, he also received a reference file showing previous reports on the consumer. "He should peruse the file, garnering out of the file what would be pertinent to the thrust of his upcoming investigation." (Bresnahan 601).

589. If an underwriting report was requested on someone on whom a claim report had previously been prepared, the claim report was provided to the field representative along with consumer reports previously prepared on the same person (Trotochaud 6437, Burge 5097–98). It was permissible for the field representative to state in the consumer report that a prior claim report had been prepared (and the customer and date) and to state the doctor, hospital dates of confinement, and the cause (Finding 241). In addition, the field representative could use the medical information in the claim report as a tip or lead in conducting his investigation for the consumer report (Finding 241).

590. Actual use of claim report information went beyond respon-

[226] Respondent stated that the record is unclear as to whether Mrs. Williams was interviewed in connection with this reinvestigation or at the time of the reopen (RPF 971b). In either event, however, notice to the insurance company following contact with Mrs. Williams was inadequate.

dent's instructions. One field representative testified that when he had recently prepared a claim report on someone he was currently preparing a consumer report on, he quoted freely from the claim report (Tr. 4032). Two other field representatives testified that they asked leading questions to confirm medical information obtained from claim reports, *e.g.,* "Has he recovered from his heart attack?" (Tr. 379) or "I understand he had a heart attack last summer." (Tr. 2888). [213]

591. Respondent used information from its claim reports in consumer reports (Findings 588–90). Respondent did not consider claim reports to be subject to FCRA and did not observe certain provisions of FCRA with respect to them (Respondent's Response to Complaint Counsel's Request for Admissions of Fact, dated May 10, 1974, No. 66).

592. Similarly, information in previous consumer reports was referred to in connection with the preparation of current claim reports. Prior to October 12, 1972, it was permissible to use record information from a previously prepared consumer report in a current claim report. Other information from a consumer report was to be reconfirmed before it could be used in a claim report (Trotochaud 6416). After the fall of 1972, field representatives were prohibited from directly quoting in claim reports, information from consumer reports, but the information could be used as a tip (see RX 658, 659; Trotochaud 6415–18).

593. Respondent used consumer report information in its claim reports (Finding 592). Such use violated Section 604 of FCRA, which specifies the permissible purposes for which consumer reports may be furnished.

594. In May 1974, respondent directed all branch offices to change their filing systems and to immediately begin filing claim reports in separate files from those of underwriting reports (see Finding 243). A directive setting forth a program to separate all existing claim files from the underwriting files was sent to the branches in June (RX 660A–H; Trotochaud 6428–29). It was anticipated that completion of the process would take a year (RX 660A, 637A). In fact, by July 30, 1975, all offices had completed the separation process (Tr. 6598).

595. Since separation of the claim and underwriting reports, claim reports have not been available to field representatives preparing consumer reports for tips or any other use (Cooke 10006–07, Baranek 9700–01).

596. With the initiation of the file separation in May 1974, field representatives were instructed that "no use should be made of non-

claim files on current claim reports or vice versa." (RX 637A, see also 637B–C; Trotochaud 6425–28). [214]

Discussion

This is a proceeding brought under the Federal Trade Commission (FTCA) and Fair Credit Reporting Acts (FCRA). The allegations of the complaint have been summarized above and that summary need not be repeated here (see pp. 2–6, *supra*). A discussion of the more significant factual and legal issues follows. It may be noted that there have been numerous court decisions construing FCRA in the course of ruling on disputes between individual members of the public and consumer or credit reporting companies. This case, however, is the first case raising important questions concerning administrative enforcement of compliance of FCRA by the Federal Trade Commission and the interrelation of enforcement between FCRA and the FTCA.

Allegations that Respondent's Employees Have Misrepresented Their Identity (Paragraphs 5–6 of the Complaint)

Paragraphs 5 and 6 of the complaint allege essentially that respondent's investigative personnel have, in certain instances, misrepresented to consumers that they are agents or employees of the companies to which the consumers have applied for benefits such as an insurance company and/or that the information furnished by consumers or others during the course of interviews will be used exclusively by the companies to which the consumers have applied for benefits. It is further alleged that certain consumers interviewed would have chosen to provide the information directly to the company from which benefits were sought rather than to respondent had they known the true identity of respondent's employees or had they known that such data would be added to respondent's files for future reference. [215]

The record shows that certain field representatives, who did not identify themselves as employees of respondent, used introductions such as that they were "from", "with" or calling "for" the company to which the consumer was applying for a benefit. Such introductions had the capacity and tendency to mislead consumers into the belief that the field representatives in question were employees or agents of the company to which application had been made for a benefit or an insurance policy (Findings 162, 163). Such misrepresentations are material to consumers contacted by respondent's investigators (Finding 164).

The record fails to show that respondent affirmatively misrepresented that it did not keep file copies of the reports or that information furnished during an interview would be used exclusively by the company to which the consumer had applied for a benefit such as insurance. However, where the introduction misled consumers into believing that they were talking to an employee or agent of an insurance company, it also had the capacity to mislead consumers to the belief that the information obtained would be used exclusively by the requesting company. In that context, the failure to disclose that a third party would retain files which might be used in connection with other transactions constituted the failure to state a material fact and was misleading (Finding 165).

A simple prohibition against the direct or indirect representation that respondent's investigative personnel are agents or employees of the company to which the consumer has applied for a benefit will adequately prevent recurrence of the violations demonstrated in the record. The evidence in this record permits no findings as to consumer beliefs with respect to the retention and use of information secured by consumer reporting agencies in those instances where proper identification was made. Accordingly, the record will not support the imposition of an order requiring affirmative disclosure that a copy of the information will be retained in respondent's files for future reference. [216]

Complaint counsel propose requiring a written disclosure which the consumer may keep, stating the field representative's name, that he is an employee of respondent, the purpose of the investigation, the person ordering the investigation and that a copy of the information will be retained in respondent's files for future reference (CB App. C, pp. 2–3). The law violations demonstrated by the record with respect to introductions on the part of certain of respondent's employees do not demonstrate so flagrant or engrained a pattern of deception as to justify this provision. It will not be adopted.[227]

Respondent argues that the procedures employed by consumer reporting agencies have been sanctioned by FCRA and that, as a result, absent affirmative misrepresentation, no order can issue (RB 10–11). Affirmative misrepresentation is not prerequisite to an order directed to these practices. FCRA does not sanction interview practices which have the capacity to deceive.

In determining the meaning of advertisements or other represen-

[227] To a considerable degree, the failure by respondent's personnel to identify themselves was occasioned by the confusion engendered by the name Retail Credit when the interview was in connection with an insurance investigation not involving credit, *e.g.*, insurance. To avoid the requisite explanations, respondent's field representatives would omit the name of their employer. The incentive to engage in such practices has been reduced by respondent's name change to Equifax (Findings 160–61).

tations, the important criterion is the net impression that is likely to be created on the general populace. *National Bakers Services, Inc.* v. *FTC,* 329 F.2d 365, 367 (7th Cir. 1964). In ascertaining the impression created, the Commission need not look to the technical interpretation of each phrase; it may look to the overall impression likely to be made. *Murray Space Shoe Corporation* v. *FTC,* 304 F.2d 270, 272 (2nd Cir. 1962). A statement may be deceptive even if the constituent words may be literally or technically [217]construed so as not to constitute a misrepresentation. *FTC* v. *Sterling Drug Inc.,* 317 F.2d 669, 674–75 (2nd Cir. 1963). And, representations capable of two meanings, one of which is false, are misleading. *Rhodes Pharmacal Co.,* v. *FTC,* 208 F.2d 382, 387 (7th Cir. 1953), *modified on other grounds,* 348 U.S. 940 (1955).

The identification by a field representative such as that he appears "from" or "for" an insurance company may be literally true in the sense that the interview is made at the request of respondent's customers. However, such an identification coupled with the failure of the field representative to identify himself as one of respondent's employees had the capacity to create the misleading impression that he was an agent or employee of the insurer. Under those circumstances, there is no need to find that there has been affirmative misrepresentation concerning respondent's retention and use of the information obtained. The Commission may, where ambiguous introductions have the capacity to mislead, ban such practices. Misleading and confusing interview techniques are not authorized by FCRA.

Requiring respondent to cease using misleading or ambiguous introductions will in no way preclude respondent from engaging in any of the activities permitted by FCRA. Such a prohibition will not preclude respondent from maintaining files as authorized by the Act. Nor will it impede the free flow of commercial information. It will merely ensure that consumers giving information do so with knowledge that they are dealing with a third party consumer reporting agency.

Applicability of the McCarran-Ferguson Act Exemption to the Practices Challenged Under Paragraphs 7–8 and 11–13 of the Complaint

Paragraphs 7 and 8 of the complaint allege essentially that respondent's investigative personnel have misrepresented the purpose of interviews by representations such as that a credit check was being conducted when, in fact, in certain instances, the purpose was to evaluate a consumer's claim for loss [218]or injury under an

insurance policy and the primary object of the interview was to observe the consumer's appearance and his mental or physical capacity in connection with such claim.

Paragraphs 11, 12 and 13 of the complaint allege essentially that respondent, through the use of certain medical authorizations obtained from insurance companies, represented directly or by implication to medical personnel that the data sought pursuant to such authorizations was for the exclusive use of such insurance companies. The complaint also alleges that consumers executed such authorizations on the basis of that belief. The complaint further alleges that, in truth and in fact, the information was not obtained for the exclusive use of the insurance companies to which the authorizations were executed but that it was also retained by respondent and, in certain instances, utilized in the preparation of subsequent reports for different customers of respondent. The complaint alleges that some customers would not have authorized the release of such confidential information had they known it would be utilized by a third party.

Respondent's claim interview procedures and utilization of authorizations to secure medical information violated Section 5, FTCA (Findings 180, 252–55). Respondent's decisions to eliminate the retention of its underwriting medical history reports in November 1973, and to eliminate the retention of claim medical reports in December 1975 (Findings 239, 244, 256) appear to give effective assurance of cessation of the acts charged under paragraphs 11–13 of the complaint. The threshhold question, however, is whether the Commission has jurisdiction to challenge such practices.

Respondent asserts the Commission has no jurisdiction to issue an order in the case of these practices because of the provisions of the McCarran-Ferguson Act (15 U.S.C. 102(b)) exempting insurers from regulation under the Federal Trade Commission Act. [219]

For the exemption to become operative, there must be findings (1) that the business is that of insurance, namely, that the industry acts as a risk-bearer for a premium; (2) that the challenged activities relate to the act of risk-bearing; (3) that the states have regulatory authority to govern the challenged activity; and (4) that state regulation is adequate. *American General Insurance Company,* 81 F.T.C. 1052, 1056 (1972). The primary question in determining the applicability of the exemption is whether the particular practice concerns the business of insurance. *Proctor* v. *State Farm Mutual Auto Insurance Co.,* 406 F. Supp. 27, 29 (D.D.C. 1975), *affirmed,* 5 CCH Trade Reg. Rep. ¶61,481 (D.C. Cir. 1977).

The prime issue in this case is whether respondent's claim

investigations and the introductions made pursuant thereto and its activities in securing medical information for insurance companies are the business of insurance. Complaint counsel strongly contend that these activities are not the business of insurance but apparently do not put in issue respondent's contention that there is state regulatory authority to govern the challenged practices and that such state regulation is adequate. The discussion herein is, therefore, confined to the question of whether respondent's activities are the business of insurance.

It is clear that respondent's claim investigations are part of the business of insurance. The determination of whether a claim under an insurance policy should be paid is central to the insurance business, directly affecting the contractual relationship between the insurance company and its policyholder even in those instances where the claimant is a third party. As a result, respondent's activities are subject to state regulation when it conducts claim investigations. This includes the introduction utilized by respondent in claim investigations; namely, the so-called indirect interview. See *Proctor* v. *State Farm Mutual Auto Insurance Company, supra,* holding that the adjustment and settlement of insurance claims is the business of insurance. Claim investigations are an integral part of that process. [220]

Respondent's acquisition of medical information through the presentation of authorizations secured from insurance companies also constitutes the business of insurance. Obtaining information by insurance companies to investigate the risk of loss prior to deciding whether to accept the risk is a part of the business of insurance. *Schwartz* v. *Commonwealth Land Title Insurance Company,* 374 F. Supp. 564, 574 (E.D. Pa. 1974).

It is immaterial that respondent itself is not an insurer as long as its activities constitute the business of insurance. The McCarran-Ferguson exemption is "not strictly limited to insurance companies . . . it is the 'business of insurance' with which the Act is concerned." *Royal Drug Co.* v. *Group Life and Health Ins. Co.,* 415 F. Supp. 343, 350 (W.D. Texas 1976). In performing this service, respondent has become an integral part of the overall scheme of insurance coverage which is regulated by state law. Cf. *Royal Drug Co., supra.* Under the circumstances, it is immaterial that respondent is selling the information under consideration to insurers.

Complaint counsel also argue that respondent's retention of the medical information and use thereof as leads or otherwise in the preparation of other reports cannot be considered the business of insurance. There is no precedent directly in point. However, it is

apparent that securing such information initially is part of the business of insurance. In many instances, insurance companies perform such functions themselves. Respondent's practices in connection with the retention of medical information and the uses thereof which might otherwise violate the Federal Trade Commission Act arise directly out of transactions subject to state regulation as the business of insurance. As best, it may be said that the activities here complained of are abuses by respondent in participating in the business of insurance. Such activities being subject to state regulation are exempt from the jurisdiction of the Federal Trade Commission to the extent regulated by state law. [221]

Allegations as to Misrepresentations of the Manner in Which Reports Were Prepared (Paragraphs 9–10 of the Complaint)

The complaint alleges that respondent has represented that its interviews were conducted in person rather than on the telephone, that direct observation of the consumers' environment was conducted, and that all sources of information listed were seen. The complaint charges that, in certain instances, interviews were conducted on the telephone rather than in person, that consumers' environments were not directly observed, and that the sources listed on the consumer report were not interviewed in person or on the telephone. The complaint alleges that users of respondent's reports would not have given as much weight to the information in such reports had the manner in which they were prepared been truthfully and factually represented.

Respondent, through its brochures, has represented that its reports, as a matter of standard or normal procedure, are compiled through face-to-face interviews of the sources listed and upon the basis of the direct observation of the field representative making the report (Findings 199–200).[228] The record further demonstrates that such representations are also apparent on the face of respondent's reports (Finding 201).

The telephone was used to some extent in the majority of respondent's reports including life and health reports, regular automobile reports and most personnel reports (Finding 185). Normally, use of the telephone was not noted on the copies of underwriting reports going to customers (Finding 194). [222]

In certain instances, reports concerning a consumer's appearance and physical environment or home surroundings were submitted, although no direct observation had been undertaken by the field

[228] Certain of respondent's reports are sold as exclusively a telephone service (Finding 183). No violation is found in connection with such reports.

representative making the report (Finding 211). The record further shows that, in certain instances, reports were submitted listing sources not seen or interviewed by the field representative preparing that report (Finding 405).

Respondent urges that no finding of deception should be made and no order entered in view of the sophistication of the audience to which the representations were directed; namely, the insurance company underwriters. Insurance company underwriters were aware of the fact that sometimes the telephone was utilized in the preparation of such reports (Finding 198; see also Finding 208).

The Commission, in evaluating promotional literature, may draw its own inferences from a reading of the advertisement. In making such findings, it need not depend on testimony or exhibits aside from the advertisements themselves. *Carter Products, Inc.* v. *FTC,* 323 F.2d 523, 528 (5th Cir. 1963); *FTC* v. *Colgate-Palmolive Co.,* 380 U.S. 374, 391–92 (1965); *Royal Oil Corp.* v. *FTC,* 262 F.2d 741, 745 (4th Cir. 1959). Respondent's brochures present no unusual problems of construction. The meaning of statements such as "You see your applicants even though you aren't able to visit each one yourself" (CX 384B) can be determined solely from the exhibits.

Insurance company underwriters may be a sophisticated audience in terms of understanding the nature of respondent's operation; namely, the telephone is sometimes used in the preparation of reports. They would not know, however, absent a disclosure on the report, whether, in a particular case, a face-to-face interview had been conducted or whether the interview had been conducted by telephone. Whether or not a face-to-face interview had been conducted or direct observation made was a significant factor in the weight to be accorded to the information in such reports, particularly where items such as physical appearance were concerned (Finding 213). [223]In view of the fact that respondent represented that face-to-face interviews and direct observation were the standard or normal procedure, the failure to give notification that they were not used in the case of individual reports, was misleading. Such disclosure will be required.

Cases such as *Waltham Precision Instrument Company, Inc.,* 61 F.T.C. 1027, 1049 (1962, *aff'd.,* 327 F.2d 427 (7th Cir. 1964) and *Sheffield Silver Co.* v. *FTC,* 98 F.2d 676, 678 (2nd Cir. 1938), indicating that advertisements are to be considered in light of the sophistication of the audience to whom the representations are addressed do not dictate a different result. The issue is not whether insurance companies or other report users have been misled into buying the service. Rather, the question is whether the failure to

note telephone use or lack of direct observation is a material fact which should be disclosed because of its potential for affecting the evaluation of individual reports. As a result, the sophistication of the underwriting industry as to how reports are prepared is not a bar to the entry of an order. In fairness to consumers, the material facts pertaining to how the individual reports were prepared or interviews conducted should be disclosed.

Allegations That Respondent Has Furnished Consumer Reports to Persons Which It Has No Reason to Believe Intend To Use Such Data for One of the Permissible Purposes Set Forth in Section 604, FCRA (Paragraphs 16–17 of the Complaint).

The complaint in paragraphs 16 and 17 alleges that respondent has furnished consumer reports to persons it had no reason to believe intended to use such data for one of the permissible purposes set out in Section 604 of FCRA. The proof pertaining to these allegations is concerned with respondent's Voluntary Follow-up Service and its Monetary Savings Program. [224]

In the case of the Voluntary Follow-up Service respondent transmitted to certain customers to whom a prior consumer report had been furnished, additional adverse information on the individual who was the subject of the report. Voluntary information generally consisted of public information found in newspapers or public records; it could also include information secured by the field representatives in subsequent investigations and during the course of preparing different reports (Findings 258–59, 261).

Under the Monetary Savings Program, respondent also, in certain instances, transmitted to its sales force information about subjects of previously prepared reports. This was done if it was discovered that an event had occurred which would cause an insurance company a loss, if such insurance company had earlier been furnished with one of respondent's reports which would have allowed it to identify such risk and to rate or decline the application of the subject of the report (Finding 264).

The Monetary Savings Program and the Voluntary Follow-up Service differed in that the initial report preceding the voluntary follow-up did not identify a risk or hazard (Finding 264 n. 87). Information under the Monetary Savings Program consisted primarily of information of a public nature such as newspaper clippings as well as police and court records; it could also be derived from subsequent investigations conducted by respondent (Finding 266).

The record further shows that respondent knew or should have known that information furnished under the Voluntary Follow-up

Service and Monetary Savings Program was sometimes furnished to insurance companies who had no insurance policy on the individual involved and who were not at that time considering an insurance application on the individual (Finding 268).

1. The Voluntary Follow-up Service

Respondent contends that the Voluntary Follow-up Service was part of the same package as the original investigation and that it is unrealistic to contend that the follow-up portion of the service served an impermissible purpose (RB 57–58). [225]

Respondent further contends that the Voluntary Follow-up Service has been held valid by judicial precedent citing *Middlebrooks* v. *Retail Credit Co.*, 416 F. Supp. 1013 (N.D. Georgia 1976). In that decision, the court expressly noted that there was an ongoing relationship between the subject of the Voluntary Follow-up Service and the insurance company to which this information was transmitted. This case is not controlling here.

Respondent contends that there is no violation of the statute in the instance of the Voluntary Follow-up Service, because Section 604 does not require absolute certainty on the part of the consumer reporting agency that the person to whom the information is transmitted has a permissible purpose for such data. The statutory standard is that before such data is transmitted, the person transmitting it must have "reason to believe" that the information will be used in accordance with the criteria set forth therein.

The record shows that insurance companies to whom voluntary information was transmitted sometimes had a policy in force in connection with the individual who was the subject of the service and at other times did not (Finding 263). Under the circumstances, the transmittal of such information without a specific request, therefore, does not meet the requirement that respondent had reason to believe that it would be used for a permissible purpose.

Finally, respondent argues that the Voluntary Follow-up Service was discontinued as of April 29, 1974, and, as a result, no order should issue. The argument is rejected. Discontinuance does not necessarily preclude the issuance of a cease and desist order. An order to desist from an abandoned practice is in the nature of a safeguard for the future. *Clinton Watch Company* v. *FTC*, 291 F.2d 838, 841 (7th Cir. 1961), *cert. denied*, 368 U.S. 952 (1962). See also *Spencer Gifts, Inc.* v. *FTC*, 302 F.2d 267 (3rd Cir. 1962). An order prohibiting this practice will issue. [226]

2. Monetary Savings Program

Respondent argues that its Monetary Savings Program is not within the scope of Section 604 since the information furnished to its customers thereunder is transmitted solely as a promotional device to illustrate the value of respondent's services. Respondent contends that the information furnished under the Monetary Savings Program cannot be considered a consumer report because it is not transmitted in connection with a determination of a consumer's eligibility for benefits. It argues that FCRA does not forbid a consumer reporting agency to disseminate information which does not constitute a consumer report.

It should be noted at the outset that the information submitted under the Monetary Savings Program is furnished only on consumers with respect to whom a report has previously been submitted. Where respondent submitted additional information to show that its first consumer report had been of value, the second submittal is necessarily relevant to the first transaction. Accordingly, respondent's promotional purpose in disseminating such material is not inconsistent with the finding that they are consumer reports although submitted for impermissible purposes.[229] In this connection, it is significant that neither the Voluntary Follow-up Service nor the Monetary Savings Program are confined to newsclippings or information from the public records. Information developed in subsequent investigations and consumer reports can also be used for such purposes (Findings 261, 266).

In the case of the Monetary Savings Program, prior to submitting such data, respondent had already submitted an unfavorable report on the individual. As a result, it was on notice that the subject of the report may already have been denied the policy applied for. It was, therefore, also on notice that the insurance companies to which the monetary savings information was submitted may not have had a permissible use for the information volunteered as a promotional device. [227]

Respondent urges that complaint counsel have failed to show both in the case of the Voluntary Follow-up Service and the Monetary Savings Program that harm to the consumer has resulted from operation of the service. The contention is not relevant. The statute unconditionally prohibits the transmission of consumer reports except for the purposes specified in Section 604. There is a presumption of harm if the statute is violated.

Respondent also urges that the information transmitted under the Monetary Savings Program is commercial speech protected by the

[229] Dissemination of consumer report information for promotional purposes is not one of the purposes sanctioned by Section 604.

First Amendment and that an order may not be issued for that reason. The First Amendment argument, to a considerable degree, rests on the assertion that respondent, under the Monetary Savings Program, does no more than transmit public record information. This is not necessarily the case. As already noted, information secured during subsequent investigations on the subject of the original report and set forth in additional consumer reports are also within the scope of the program. The argument that respondent does no more than transmit information in the public domain is, therefore, not dispositive of the issue.

The Act's Statement of Finding and Purpose expressly notes that there is a need to ensure a respect by consumer reporting agencies for the consumer's right to privacy (Section 602(a)(4)).[230] Clearly, Section 604's limitations on the dissemination of consumer report information are designed to protect that right. [228]

As respondent states, commercial speech, like other speech, is protected by the First Amendment. *Virginia State Board of Pharmacy* v. *Virginia Citizens Consumer Council, Inc.*, 425 U.S. 748, 770–72 (1976). However, this does not mean that commercial speech can never be regulated (ibid).[231] "[B]ecause of the 'commonsense differences' between commercial speech and other varieties, even commercial speech subject to First Amendment protections may nonetheless enjoy a 'different degree of protection' than that normally accorded under the First Amendment." *Warner-Lambert Co.* v. *FTC,* Slip Op. p. 2 (D.C. Cir. Sept. 14, 1977) [11 C.D. 601; 562 F.2nd 749 (1977); *cert. denied,* Apr. 3, 1978].

FCRA "supports and protects a significant personal right, the right to privacy." *Millstone* v. *O'Hanlon Reports, Inc.*, 528 F.2d 829, 833 (8th Cir. 1976). In enacting Section 604's requirement that consumer reports be furnished for a permissible purpose, Congress struck a balance between the individual's right to privacy and the consumer reporting agency's freedom to disseminate information. Congress had the power to strike that balance. As the 8th Circuit noted, "consumer credit reports are not protected speech for which under the First Amendment 'Congress shall make no law.' " The First Amendment does not bar the issuance of an order in connection with respondent's challenged practices under the Monetary Savings Program.

The Order will prohibit respondent from submitting consumer

[230] See also Senate Report No. 91–517 (91st Cong. 1969, p. 1), stating "[t]he bill also seeks to prevent an undue invasion of the individual's right of privacy in the collection and dissemination of credit information."

[231] The court, in *Virginia State Board of Pharmacy,* noted that the attributes of commercial speech, including such characteristics as greater hardiness and objectivity may also make inapplicable the prohibition against prior restraints (425 U.S. *supra* at 771 n. 24).

reports to persons who it has no reason to believe intend to use the information for a permissible purpose as set forth in Section 604 of the Act. The Order will further prohibit respondent from disseminating consumer report information unless there is a specific request therefor. [229]

Allegations That Respondent Has Reported the Existence of Adverse Information in Violation of Section 605, FCRA (Paragraphs 18–19 of the Complaint)

The allegations that respondent has reported obsolete information violative of Section 605 pertain to respondent's employment and motor vehicle reports.

In connection with the employment reports, the parties have stipulated as follows:

> When respondent is requested to prepare employment reports covering employment experience for more than seven years and when respondent obtains adverse information more than seven years old from a former employer, as a matter of established procedure or usual and customary practice, respondent states in the reports "In compliance with the FCRA, no additional information can be reported from this former employer covering employment experience prior to seven years ago" or otherwise indicates that the Fair Credit Reporting Act does not permit the reporting of such information.
> (CX 1445D.)

The sentence "In compliance with the FCRA, no additional information can be reported from this former employer covering employment experience prior to seven years ago" is used *only* in connection with reports containing adverse information. This compels the inference that it is used to signal the existence of adverse information in violation of Section 605, FCRA (Finding 272).

Respondent attempts to justify the use of the stock sentence in question. It asserts that "[r]espondent cannot be expected to lie by advising the customer that all the information developed was favorable, nor to write artfully ambiguous reports that seek to conceal the existence of unfavorable data", in the case of those [230] reports where employers have requested a report exceeding 7 years (RB 68). A prohibition on this practice, however, would not, as respondent asserts, require it to issue deceptive or misleading reports. To prevent misunderstanding, respondent could simply notify the users of such reports of the limitations imposed by the Act on the reporting of obsolete information. The record demonstrates no need to disclose those limitations only in the case of those reports where adverse information over 7 years old has been developed.

The use of the stock sentence does disclose an item of adverse

information although the details are not set forth. The subject of a report where such a stock sentence is included, moreover, might well be in a worse position than a consumer with respect to whom a report spells out the details of the adverse information reported. In that case, at least the consumer is in a position to take advantage of the disclosure requirements of the Act and to dispute the items in question where appropriate. Such remedies are not available to the consumer when boilerplate language is used to signal the existence of adverse information, but the details are not disclosed.

The fact that complaint counsel has failed to introduce evidence of injury to consumers in specific instances is irrelevant. The practices under consideration violate the statute. Congress, in enacting Section 605, determined that reporting of obsolete information is harmful to the consumer. There is no need to duplicate the legislative finding on that score in an adjudicative proceeding.

Respondent objects that there has been a failure of proof. It asserts complaint counsel failed to show that any single employment report forwarded by respondent containing the stock sentence in question was transmitted in connection with an individual considered for a job at [231]an annual salary below $20,000.[232]

The argument is without merit. The parties have stipulated that the stock sentence in question is used as a matter of established procedure. It would have made no sense for respondent to establish the procedure; namely, to issue such warnings to users of reports, in connection with employment reports for jobs involving salaries at or greater than the $20,000 level. In the case of those reports, respondent is at liberty to report adverse information more than

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[232] Employment reports concerning prospects for jobs for $20,000 or more a year are exempt from the requirements of Section 605(b) prohibiting the reporting of certain items of obsolete information. The section provides in relevant part:

(a) Except as authorized under subsection (b), no consumer reporting agency may make any consumer report containing any of the following items of information.

(1) Bankruptcies which, from date of adjudication of the most recent bankruptcy, antedate the report by more than fourteen years.

(2) Suits and judgments which, from date of entry, antedate the report by more than seven years or until the governing statute of limitations has expired, which ever is the longer period.

(3) Paid tax liens which, from date of payment, antedate the report by more than seven years.

(4) Accounts placed for collection or charged to profit and loss which antedate the report by more than seven years.

(5) Records of arrest, indictment, or conviction of crime which, from date of disposition, release, or parole, antedate the report by more than seven years.

(6) Any other adverse item of information which antedates the report by more than seven years.

(b) The provisions of subsection (a) are not applicable in the case of any consumer credit report to be used in connection with—

* * * * * * *

(3) The employment of any individual at an annual salary which equals, or which may reasonably be expected to equal $20,000, or more.

seven years old. Under the circumstances, the inference is inescapable that the procedure was intended to apply in the case of employment reports not within the exemption of Section 605(b)3. Complaint counsel were not required to prove such occurrences in specific instances. It is the function of stipulations between the parties to eliminate the need for such proof.

The Order will prohibit the practice. [232]

Complaint counsel's allegations that by masking out obsolete information on motor vehicle reports, respondent has reported obsolete information contrary to the provisions of Section 605 has not been sustained. The evidence indicates that to the extent that this practice occurred, it was because certain State Motor Vehicle Departments continued to report such information despite the provisions of FCRA. The evidence further indicates that respondent attempted to persuade the state authorities to modify their practices in this respect (Findings 274–79).

The record demonstrates that with respect to the motor vehicle reports, there was no reasonable alternative to the practices followed by respondent in masking out the old information (Finding 279). Under the circumstances, respondent's practices in connection with motor vehicle reports are not considered violations of the statute justifying the issuance of an order. [233]

The Reasonable Procedures Allegations (Paragraphs 20–21 of the Complaint)

The allegations that respondent has failed to conform to the requirements of Section 607(b) of FCRA, providing that a consumer agency, whenever it prepares a report, shall follow reasonable procedures to assure maximum possible accuracy are central to this proceeding. A major part of the effort of litigating the case has been devoted to those charges.[233]

Complaint counsel has attempted to prove these allegations by showing that the interaction of production requirements, compensation system, time pressures on field representatives, the requirements for production of adverse (protective/declinable) information and financial pressures on branch offices may result in the production of inaccurate reports. This phase of the Commission's case relies primarily on the testimony of a number of ex-employees and internal Company documents. The proof on the reasonable procedures issue relies essentially on evidence pertaining to respondent's

[233] Section 607(b) provides "'[w]henever a consumer reporting agency prepares a consumer report it shall follow reasonable procedures to assure maximum possible accuracy of the information concerning the individual about whom the report relates."

general procedures. It is, therefore, necessary to look at respondent's system as a whole.

The record shows that a substantial number of respondent's employees were unable to meet their production requirements of completed cases within a normal day or workweek in compliance with Company procedures. As a result, some resorted to shortcutting techniques with the result that inaccurate reports were produced. Such practices were principally the listing in reports of sources not actually contacted by respondent's field representatives, falsification of the time coverage,[234] the failure to see logical sources, that is, sources that are in a logical position to give the information desired, and failing to ask a full range [234]of questions. Other field representatives have found it necessary to put in large amounts of overtime.

The record also shows that many and perhaps the majority of respondent's field representatives are able to produce the number of cases required in accord with Company procedures. That, however, does not demonstrate the reasonableness of the system where it is apparent that a substantial minority cannot cope.

In some instances, respondent has attempted to demonstrate that the field representatives testifying in the Commission's case were too disorganized or for other reasons were unsuitable to do the work. Even if this were the case, that would constitute no defense to the charges. If such persons are employed, then the system is simply not designed to produce maximum possible accuracy. If, as the record indicates, respondent employs substantial numbers of field representatives who cannot cope with the system as it exists, then such procedures are unreasonable for that reason alone.

The second major aspect of the Commission's case on reasonable procedures is the allegation that respondent imposed quotas for the production of adverse or protective/declinable information.[235]

Respondent urges that its system of home office audits measuring the development of adverse information by branch offices was an educational or training tool to improve report quality and was not used for policing purposes (RRB 69). The quality audits were used as a departure point for determining whether field representatives in a particular unit were employing proper investigative techniques such as asking the proper range of questions, getting a sufficient number of direct interviews with the subjects of reports, and seeing appropriate sources. It is also true that if a field representative consistently failed to develop any adverse information, [235]there could be a

[234] The time that a source has known the subject of the report.

[235] For definition of protective/declinable information, see Findings 281–82.

legitimate question as to his performance on the job. Nevertheless, in practice, the system of home office audits was not a reasonable procedure designed to assure maximum possible accuracy. Scoring well in the audits became an end, in and of itself, as is made evident by respondent's internal memoranda.

Respondent's employees have been told, in connection with such audits, that it is the production of protective/declinable data which keeps respondent in business (Finding 309) and respondent's employees in the field are extremely sensitive to the analysis results, good or bad, which "have a definite effect on the Manager's morale, the Manager's individual bonus, and the morale of the [employees]." (CX 766; Finding 310). And officials sought the right wording to get the decline across when such audits were made (CX 775). Moreover, offices and regions competed with each other with respect to the ranking in such audits (Finding 311).

The fact that review of branch office performance with respect to production of adverse information was not quality control unalloyed is evidenced by the following:

> . . . the service is quite marketable that you are producing although *we want to consistently look for ways and means of getting more and more declinable information into our reports* and you are well aware of this. (Regional Vice President to manager, Miami office, February 17, 1972, subsequent to review of cases in an office visit, CX 494A).

The record shows that in the relevant period, respondent's branch offices were under systematic scrutiny concerning their performance in the production of adverse, *i.e.,* protective/declinable information through the home office audit procedure. The record shows that branch offices were ranked in thirds against companywide averages for the preceding year relating to the production of such information and that branch management was under considerable pressure to score well in [236]those rankings. Field representatives were also pressured to produce protective/declinable information so that their offices would score well.[236]

The quality audit system ranking a branch office's performance in the production of protective/declinable information against all other offices in terms of upper, middle and lower thirds computed on the basis of organizationwide figures for the preceding year, impliedly set quotas for the production of such information (Finding 343).

Pressure on field representatives to produce protective/declinable

[236] *E.g.,* a field representative with a poor showing in producing adverse information was told that with such a performance in the next audit, he "would actually pull the office down instead of helping it." (CX 1199, Finding 319). And, branch offices with a lower third ranking have been told that they were pulling the region's percentages down considerably (CX 1222A; Finding 318).

information took diverse forms, respondent's branch managers having considerable discretion in running their offices. For example, one branch manager threatened to withhold raises; in two offices, charts of individual field representatives' production of protective/declinable information were kept. In another office, field representatives received monthly sheets from the branch manager indicating whether their production of protective/declinable information was at an appropriate level (Findings 319, 321).

There is persuasive evidence of significant pressure on field representatives to meet certain minimums in the production of protective/declinable information (see generally, Finding 319). Consider the following communications: [237]

DECLINES: Some of our folks were on the lower 'rung' and are improving. We have no one below 6.6% in Decline in Life or 6.7% in Auto. Congratulations to Coble, Cundey, Landwehr, and Ursish for over 10% decline Life and to the majority of our people for over 10% decline in Auto. Attached are the statistics for your review.

(Manager, Dayton branch office in Monthly Newsletter to suboffices, February 1974, CX 742B).

* * *

Phil, our objective on protective is 21% and our objective on declinable is 5% . . .

(Manager, St. Paul office to field representative, April 4, 1973, CX 1200).

* * *

. . . It is very gratifying to see the increase of your declinable cases and I am extremely pleased with the Special Life feature of 9% declinable. The Narrative declinable of 4% has just met company objectives and I would like to see this increased, if at all possible in the coming months.

(Supervisor, San Mateo office to field representative, May 9, 1973, CX 1246A).

Communications of this nature make clear the percentages constituting acceptable objectives or levels of performance. Moreover, such memoranda within a year of each other from separate and geographically dispersed offices compel the inference that the practice was substantial.

Such evidence is not vitiated by general testimony that no quotas were in effect. It may be that some field representatives were only told they should obtain "some", and not specific percentages, of such information. However, the contemporaneous documents show that instances did occur where specific percentages were directly or

impliedly set. The fact that such pressure may not have [238]been put on all field representatives does not insulate the practice from remedial action.

The record does not demonstrate an overall pattern of overt sanctions such as firings or the withholding of salary increases or promotions as penalties for the failure to achieve specific levels of protective/declinable information.[237] The pressures as far as can be determined from this record, were generally more subtle: for example, achievement in production of protective/declinable information as measured by the audits was one factor considered in connection with managerial incentive bonuses and field representatives put down the objective of achieving particular percentages of protective/declinable information on their personal appraisal forms (Findings 310, 320, n. 106). And, field representatives' performance on the quality audits was one factor among several to be considered in salary recommendations by the branch manager (Finding 313).

The following statement by one of respondent's ex-employees appears to give a fair summary of what frequently occurred: [239]

> At the end of every month, I was reminded that I didn't have the office objective of percentage of protective information by the supervisor and that I really ought to try a little harder to get it. There was always implication that there would be some consequences. but there were never any consequences. I have no idea what the consequences would have been.

(Farra 754.)[238]

Although the pressure on many individual field representatives may have been informal, such procedures are not reasonably designed to achieve maximum possible accuracy.

Branch offices were scored on audit samplings too small to be a fair test of their performance, and they were competitively ranked against companywide averages for the preceding year with no showing that such yardsticks could be validly applied to all the offices measured, and praise and blame accurately apportioned on the basis of such audits. Such practices have the potential for inaccurate reporting (Findings 340–41).

The potential of the quality audit system to adversely influence

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[237] The record is mixed. There is evidence that one supervisor was demoted when his unit did not pass an audit (Crepeau 1765–66), that another was put on probation for similar reasons (RX 446) and that in the Newark office, field representatives were told that salary increases would be withheld until declinable objectives were met (CX 1283A). On the other hand, the supervisor who was put on probation, RX 446, *supra*, was given a bonus to which he was not mathematically entitled although his unit did not meet the corporate average of 4 percent of such information on a consistent basis (Eldred 11261–62, 11327). And, managers whose offices were ranked in the lower third on home office quality audits have, nevertheless, been promoted (*e.g.*, Foley 11510).

[238] This field representative testified that such pressure had no effect on the manner in which he prepared reports (Tr. 755).

report writing is perhaps best set forth in some of respondent's internal memoranda:

> We did have cases in the analysis which would have been graded decline, except for a slight change in the terminology the field representative used.

(CX 775.) [240]

Another memorandum noted, "We notice a continued tendency to use the phrases, 'it is believed', or 'sources believe.' Try to eliminate this and just give the specific information without these comments, which tend to disturb the confidence of the underwriter in our report." (CX 1565A). In another memorandum, a branch manager was disturbed because field representatives stopped short of answering the final question or glossed over detrimental information with comments such as that a "man was a good driver or had no personal criticism" or "some good pat on the back or fine recommendation which overshadowed good decline information." (CX 1340).

The pressure to withhold information from reports which could put into perspective detrimental information because of the desire to score well in audits has the clear potential for harm to the consumer. Similarly, the injunction to eliminate phrases such as "it is believed" has the potential to increase the impact of adverse information to the detriment of the consumer. There is a distinction between knowledge and belief. If phrases such as "it is believed" or "sources believe" affect the confidence which underwriters place in reports, they should be kept in the reports for precisely that reason.

It makes no difference that the elimination of such phraseology might not lead to literal misstatements. It must be recognized in this connection that much of the information which respondent reports is not purely factual in the sense that it can be definitely resolved as, for example, age, duty, identity, marital status, etc. (RX 107Z–170). Rather, a great deal of the information reported by respondent in areas such as health, habits, and reputation is subjective where judgment must be exercised and which may be matters of opinion (RX 107Z–170, 102Z–17; see also Tilden 11854). In fact, respondent expressly recognizes that differences of opinion are possible in these areas (RX 107Z–170). The degree of a source's confidence in such information is clearly a crucial consideration as are any factors which may mitigate unfavorable information. The potential harm to consumers from injunctions to delete qualifying phrases such as "it is believed" or statements like "a man was a good driver or had no personal criticism" is patent in areas such as habits or reputation where subjective judgment must be exercised. [241]

Respondent contends that complaint counsel have not made the threshold showing necessary to demonstrate a violation under Section 607(b). They assert that complaint counsel have not introduced one report with respect to which there has been shown any inaccuracy caused in whole or in part by respondent's salary and production system. In short, respondent urges that the question of reasonable procedures is not reached unless there is a showing of specific inaccurate reports resulting from the procedures under consideration. Respondent, in this connection, relies upon a number of judicial precedents refusing to strike down a procedure as unreasonable under Section 607(b) if the reports under consideration were not found to be inaccurate, *e.g., Peller* v. *Retail Credit Co.,* 359 F.Supp. 1235 (N.D. Ga. 1973), *aff'd. mem,* 505 F.2d 733 (5th Cir. 1974). Those cases are not controlling here. They involve attempts to vindicate private rights in suits for damages under the Act. Clearly, there can be no damages to an individual if no inaccuracy has been shown in the particular report.

The Federal Trade Commission, in its role of administratively enforcing the Act, has a broader function. It need not rely on inaccuracy in specific reports. It may scrutinize respondent's procedures generally to determine whether they are reasonably designed to assure the maximum possible accuracy of information concerning the individuals with respect to whom the agency's reports relate. Here, the record shows that production requirements, time pressures and respondent's quality audit system have the potential for resulting in inaccurate reporting.

To the extent that reports are prepared listing sources not seen with unqualified sources contacted, time coverage misstated, or insufficient time taken to ask the applicable questions, such methods are likely to result in inaccurate reporting. Pressure as to report wording to facilitate good audit scores may have similar results. As already noted, respondent's quality audit system, when it was in effect, implicitly set quotas for the production of adverse information. The Commission may evaluate respondent's procedures as a whole to determine whether a consumer agency is following reasonable procedures to assure maximum possible accuracy without a case-by-case analysis of a myriad of reports. [242]

Respondent, in urging that the key test is reasonableness, seems to equate that concept with the Rule of Reason. Moreover, the

argument apparently implies that the required showing must be one of actual adverse effect on consumers (RB 72-73).[239] There is, however, no requirement in Section 607(b) that the Commission must permit procedures to continue until, in fact, adverse results have occurred. In this connection, Section 621 of the Act defines the Commission's enforcement role. It states, "[f]or the purpose of the exercise by the Federal Trade Commission of its functions and powers under the Federal Trade Commission Act, a violation of any requirement or prohibition imposed under this title [FCRA] shall constitute an unfair or deceptive act or practice in commerce in violation of section 5(a) of the Federal Trade Commission Act." The term "reasonable procedures" under Section 607(b) is one that requires interpretation in light of the surrounding circumstances. In Section 621, Congress accordingly linked such interpretation with the concept "of an unfair or deceptive act or practice" as set forth in Section 5 of FTCA. The Commission, in determining practices to be unfair or deceptive, need not make a finding that actual deception or injury has occurred, *e.g., United States Retail Credit Association, Inc.* v. *FTC,* 300 F.2d 212, 221 (4th Cir. 1962); *Sears, Roebuck & Co.* v. *FTC,* 258 F. 307, 311 (7th Cir. 1919). The Federal Trade Commission, moreover, is to [243]stop unfair acts and practices in their incipiency. See *FTC* v. *Brown Shoe Co.,* 384 U.S. 316, 322 (1966).[240] Under the circumstances, the Commission has the power to prohibit practices under Section 607(b) of FCRA applying the same standards as are applied under Section 5 of FTCA in declaring certain methods of competition unfair. The Commission, in this case, need find no more than that the procedures, in effect, have the potential and capacity to result in inaccurate reporting.

As a general rule, when field representatives resorted to shortcuts such as the listing of sources not seen, they did not falsify adverse information, and there is no evidence in the record of a report where adverse information has been falsified. In fact, the record shows that where sources were faked, reports were generally favorable to the consumer. This, however, does not preclude a finding that such practices violate the requirements of Section 607(b).

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[239] Respondent links the assertion that judicial precedent requires a showing of inaccuracy in specific cases with the contention that the Supreme Court, while construing Section 5 of the FTC Act, in *FTC* v. *Sperry Hutchinson Co.,* 405 U.S. 233 (1972), "stressed once again the need to show the effect of a practice on consumers before the Commission could prescribe the practice as being unreasonable under Section 5." (RB 73).

[240] In *Brown Shoe,* it may be noted, that the court held that, in a case dealing with restrictive franchising, the Commission was not required to show the element in Section 3 of the Clayton Act that the effect of the franchise program "may be to substantially lessen competition or tend to create a monopoly." The court held rather that the Commission had the power under Section 5 to arrest trade restraints in their incipiency without proof that they amount to an outright violation of Section 3 or other provisions of the antitrust laws. In this connection, it may be noted that Section 3 itself did not require proof of actual injury to competition and is itself a statute designed to stop certain practices in their incipiency.

Respondent contends that the benefits of FCRA extend only to the consumer and not the report user. The primary emphasis in the statute is on the protection of consumers with respect to whom reports are prepared. Nevertheless, the statement of findings and purpose in Section 602, makes it clear that inaccurate credit reports impair the efficiency of the banking system. In short, the Act recognizes that the public as a whole has a stake in accurate consumer reporting. Section 607(b) requiring procedures to assure maximum possible accuracy, draws no distinction between adverse and favorable reports. [244]

Finally, there is the question of remedy for the Section 607(b) violations. Complaint counsel seek essentially an order prohibiting respondents from requiring its employees to complete or prepare an unreasonable number of consumer reports.[241] or to prepare a certain proportion of consumer reports containing adverse information about the subjects of the reports (CB App. C, p. 8, par. 4(a)–(b)). Complaint counsel also request a prohibition on various sanctions with respect to compensation, promotions, or job status to compel respondent's employees to prepare an unreasonable number of reports or a certain proportion of reports containing adverse information (CB App. C, p. 10, par. 5). [245]Complaint counsel further recommend the adoption of a prohibition against emphasizing the development of adverse information in the preparation of consumer reports and failing to train its personnel to complete consumer reports "in a manner which is fair and equitable to the consumer with equal emphasis on the development of and reporting of favorable and adverse information." (CB App. C, p. 11, par. 6).

The recommended provisions will not be adopted in the form proposed. They would be difficult, if not impossible, to enforce. The prohibition against requiring production of an unreasonable number of reports would compel the Commission and its compliance staff to become involved with the details of supervising several thousand field representatives, a task for which it does not have the resources.

The variables determining what is a reasonable workload for one

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[241] Complaint counsel's order defines an unreasonable number of reports as follows:

For purposes of subparagraph 4(a) above, an unreasonable number of consumer reports shall be that number of reports which an investigator cannot, with due diligence, complete or prepare accurately while conforming to the following procedures:

(1) interviewing all the sources or other third parties listed on said reports;
(2) conducting all interviews directly and in person, unless it is clearly indicated on the report that the telephone was used;
(3) making all observations of the homes, neighborhoods, or other physical surroundings of the consumers who are the subjects of the reports directly and in person;
(4) confirming all adverse information through interviews with independent sources, unless it is clearly indicated on the report that the information was obtained from one source only.

of respondent's field representatives are numerous. They include the requirements of the preparation of particular reports, the mix of such reports assigned to the individual representative, the areas where the investigations are to be made, the ability of the individual field representative, and the production climate in a particular branch office. In addition, new types of reports placing different demands on field representatives may be instituted by respondent either on its own initiative or at the request of its customers. Accepting the definition of an unreasonable number of reports in complaint counsel's proposed order would not simplify the task. The Commission would still be required in each compliance proceeding essentially to relitigate the instant case.

The requirement of Section 607(b) mandating reasonable procedures would be more effectively enforced by requiring respondent to institute performance reviews of its field representatives on a systematic basis. The Order will require respondent, on a random sampling basis acceptable to the Federal Trade Commission, to semi-annually conduct unannounced performance reviews of its field representatives to determine whether the sources listed have been interviewed, whether the sources contacted were logical sources and whether the information was accurately recorded. The Order will further require that the results of such performance checks be submitted to the Federal Trade Commission. [246]

The results of such performance checks should disclose a pattern from which a determination can be made as to whether respondent is imposing a reasonable workload on its field representatives and where corrections may be needed. Such a provision would be essentially self-enforcing. Inaccurate reporting is in the interest of neither respondent nor its customers. Accordingly, if the required performance reviews were to show a pattern of inaccurate reporting, such as the faking of sources, respondent would have a strong incentive to change its procedures to achieve more accurate results.[242]

Complaint counsel propose that respondent be required to complete a "Source Information Analysis" for each source of adverse information contained in an investigative consumer report (CB App. C., pp. 5–6). Under this provision, respondent would be required to disclose whether the source in question gained his information through personal knowledge, personal observation or hearsay, and whether the investigator obtained such information through personal interview, telephone interview, direct personal observation or file

[242] In the event that necessary remedial action is not taken, and if the need therefor is demonstrated by the required performance reviews, then the Commission may seek modification of the Order.

information. This provision will be entered; it is related to shortcuts such as listing sources not seen and contacting unqualified sources. It is also designed to prevent deception as to whether information has been obtained by the investigator's personal observation. The disclosure required by this provision concerning the provenance of the data will facilitate the evaluation of the report by respondent's customers. Complaint counsel has, however, not made a persuasive showing that such disclosure should be coupled with further information about the number of other reports prepared that day by the field representative in question. As already noted, there are a multiplicity of variables involved in determining a reasonable workload for a particular field representative. It is unlikely that such information would facilitate customer evaluation of the report. This part of the proposed order will not be adopted. [247]

Complaint counsel's provisions with respect to the imposition of adverse information quotas will not be adopted in their entirety. The record shows that, through the home office quality audits, respondent, in the relevant period, in effect, set up a quota system for the production of adverse (protective/declinable) information, and that practice should be banned. The unreasonable pressure on branch offices and field representatives for the production of adverse information was rooted in respondent's system of home office quality audits. The prohibitions in the Order should, therefore, focus on that procedure. It was the institutionalized competition for high ranking in the quality audits which gave rise to unreasonable pressures on respondent's personnel in the field to produce certain percentages of adverse information. Prohibiting these practices should adequately bar the violations documented here.

That portion of complaint counsel's proposed order defining a prohibited system, plan or procedure will not be adopted. The provision is unduly prolix. The record does not support the inclusion of all the elements of complaint counsel's definition in the order. For example, there is insufficient evidence in the record supporting a specific prohibition against sanctions related to a field representative's compensation, job status, promotions, etc. to compel the production of such information (see CB App. C, pp. 9–11 and n. 237).

Respondent will be prohibited from compelling or inducing its investigative personnel to complete or prepare a certain proportion of consumer or consumer investigative reports containing adverse information with respect to the subject of the report by utilizing the quality audits or any similar plan or procedure.

Respondent's practice of measuring the audit results of individual branch offices against companywide averages for ranking by lower,

upper or middle thirds in the production of protective/declinable information had the potential for inaccurate comparisons because of the disparity of results to be expected among different offices because of differing economic and geographic factors. The system, therefore, had the potential for generating pressure for increased production of adverse [248]information on the basis of invalid comparisons and, therefore, was unreasonable on that score (Finding 340). In addition, the audit results for individual branch offices with respect to the production of such information were based on small samples precluding the assurance that such results were representative for the office measured. The system, therefore, had the potential for generating pressure to increase protective/declinable information on the basis of unrepresentative data and was unreasonable for that reason (Finding 341).

The Order will prohibit the utilization of any system of quality audits or any similar system, plan or procedure ranking the performance of branch offices or other organizational units with respect to the production of adverse information against company-wide or regional averages (1) unless respondent can demonstrate such averages provide a valid standard of comparison for all the branch offices or units measured, and (2) unless respondent can demonstrate that the particular audit or survey utilized includes a representative or statistically valid sample of the branch office or other unit surveyed.

Complaint counsel also seek a prohibition against emphasizing the development of adverse information in the preparation of consumer reports and failing in training, supervisory, and review procedures to inform its personnel to complete or prepare consumer reports in a manner fair and equitable to consumers with equal emphasis on the development and reporting of favorable and adverse information (CB App. C, p. 11, par. 6).

This provision will not be adopted. The proposed injunction that respondent's employees be instructed to prepare reports in a "fair and equitable manner" with "equal emphasis" on favorable and unfavorable information is too general and vague for practical enforcement. Respondent's manuals already enjoin field representatives from using words emphasizing unfavorable information out of proportion and instruct that "Rumors, gossip, and scandal must be sifted." (RX 102Z–17). Inevitably, if this provision were entered, the Commission would have to engage in the time-consuming task of analyzing numerous [249]informal contacts between respondent's management and employees involving verbal exchanges. The FTC in the past has refused to enter broad prohibitions against practices

capable of only imprecise definition (*e.g.*, excessive or unfair pressure) for similar reasons. See *Arthur Murray Studio of Washington, Inc.*, 78 F.T.C. 401, 441 (1971), *aff'd* 458 F.2d 622 (5th Cir. 1972). The Order provisions directed to respondent's quality audit procedures should remedy the violations found without the disadvantages inherent in the proposed provision.

Respondent states that regulatory action making continuation of the regular life and health reports impossible would have adverse effects on the consumer (RB 78). It states in this connection:

> if an agency were required to prepare every report using the standard of care that is appropriate to the most detailed service it furnishes, the result would be to preclude agencies from selling more than one kind of report, a result not contemplated by the FCRA.
> (RB 78.)

Apparently, respondent contends that, in the case of the lower-priced reports, a lesser standard of care is permissible. There is, however, nothing in the Act which supports an argument that those consumers only able to afford or purchasing insurance with lower limits should have less protection than those buying higher-priced policies. Certainly, the harm to the consumer is the same if erroneous information is reported concerning, for example, his habits and reputation regardless of the benefit applied for or the type of report made. Reports may differ in the depth of their coverage and the amount of detail reported depending on the price of the report. And procedures may vary to get the requisite detail depending on the depth of coverage desired. However, the standard of care with respect to the accuracy of the information actually reported should be the same for all reports. It would be anomalous to interpret this statute which expresses broad concern for all consumers as permitting a lesser standard of care for those consumers who are the subjects of lower-priced reports. [250]

In any event, the provisions to be entered here impose no burdens jeopardizing the continuation of respondent's regular reports.

Respondent's Product Cost and Effort Studies

Respondent relies on the Arthur Andersen & Co. evaluation of its product cost and effort studies and the bonus contribution computations (RX 566) to demonstrate that the field representatives' compensation and the related production requirements are reasonable. That study has been considered in weighing the conflicts in the evidence on this issue.

Andersen, to test the reasonableness of respondent's reporting

standards, reviewed the data from respondent's product cost and effort study to determine whether a field representative could work enough cases in an 8-hour workday and correspondingly in a period of three 21-day months to make his standard or quota (RX 566 IV–6).

In this connection, it further determined the evaluation should be made by applying a measure of reporting standard reasonableness that could be applied to each of the seven basic reports it had selected for this purpose on an individual basis. It selected as the criterion, "Monthly Bonus Contribution, defined as the excess of earnings credit over salary and expenses that would be earned by a field representative with a given set of reporting standards and a workload consisting solely of a given type of report." (RX 566 IV–7).

Andersen's conclusions that respondent's reporting standard is reasonable is based on its calculations of a positive bonus contribution for seven basic reports in 1973 for Code 04 offices (RX 566 F–H). In this connection, Andersen's conclusion that respondent's reporting standard is reasonable is based on the assumption that Code 04 offices are representative of respondent's entire organization (Findings 453, 490). The Code 04 offices were selected as the most representative for the organization because their averages for figures such as reporting standard, expenses, production, and earnings were closest to the Company averages (Finding 453, n. 174). Presumably, homogeneity on these points was considered essential to the determination that Code 04 offices were representative of the entire organization. [251]

There is a question, however, whether the conclusions to be drawn from the Andersen bonus contribution calculations confined to Code 04 offices validly apply to respondent's organization as a whole. The record shows that, while the Code 04 offices may be closest to the companywide averages in categories such as report production, revenue, etc., there are substantial variations in branch offices in other code classifications in this respect from both the Code 04 office averages and the organizational averages (see RX 754; Findings 480–81).

Significantly, respondent's branch offices were given different classification codes to reflect differences in cost and the difficulties of preparing reports in different areas as well as differences in prices charged to customers for the reports (Finding 452). And, respondent states, "[i]t has long been recognized, for example, that it requires more time to prepare reports in certain areas (such as a large metropolitan area) than in others (such as a small city). The number of codes, and the classification of given offices within these codes, have varied over the years as conditions change." (RPF 327). It is

336-345 O - 81 - 65

evident from the very nature of respondent's code classification system for its offices that there are significant differences in the level of effort required in preparing reports among groups of branch offices in the different code classifications.

The record (in particular, RX 566 F–H) shows that there is considerable disparity among the monthly bonus contribution for reports in the three different categories of 1973 Code 04 offices for whom Andersen made computations. Although the bonus contribution for all three is positive, the differences are substantial (Finding 478, n. 183).[243] [252]

The Andersen bonus contribution calculations for the Code 04 offices utilize an average monthly salary of $610 and a reporting standard of .505 as two of the elements in the computation (RX 566 F–H; Finding 483). The interaction of those two elements is a critical factor in the computation of bonus contribution (Finding 483). The record shows no calculations as to the impact on bonus contribution of reporting standards and salaries at ranges other than those shown in RX 566 (Finding 484). On the basis of these characteristics, there is insufficient evidence to support a finding that respondent's field representatives were sufficiently homogenous so that the averages in RX 566 could be applied generally to them throughout the organization.

The Andersen evaluation concerning the reasonableness of the reporting standard and the underlying product cost and effort studies failed to take into consideration significant factors bearing on the ability of field representatives to complete their tasks in the given time. For example, no consideration was taken of the fact that different groups of field representatives, because of variables such as geography, scheduling, mix of business and the volume of business, may differ significantly in ability to accomplish their tasks (Findings 460, 488).

If averaging is employed in studies of this nature and conclusions drawn therefrom as to units in different classifications, then a showing is required that there is sufficient resemblance between the groups to whom the conclusions are applied on the essential points (in this case, level of difficulty, reporting standards, etc.). This is prerequisite to a showing that the Code 04 averages on bonus

[243] Respondent states that the salary on RX 566 G and H was overstated and that the actual salaries applicable to each group of offices with respect to which such computations pertain were less (RPF 640). Respondent contends further that had such lower salary been utilized, the bonus contribution on RX 566 G and H would have been greater and the differences between RX 566 G and H and RX 566 F, less. The fact remains respondent was unable to provide the information necessary to substantiate this point (see Deibig testimony quoted in RPF 640). This decision must draw its conclusions from the computations actually in the record. There is no way of determining from the evidence, the extent to which the computations were affected by respondent's inability to retrieve the appropriate figures.

contributions are meaningful for all of respondent's branch offices, including those offices not within the Code 04 category. [253]

Respondent's code classification system for putting different branch offices in specific codes presupposes that there are significant differences with respect to the level of effort required to prepare reports in offices in different categories. As a result, respondent had the burden of demonstrating that despite these differences, all offices were sufficiently homogenous with respect to these critical characteristics so that the Code 04 offices could be considered as representative of the organization as a whole. That burden has not been met. The mere fact that the Code 04 offices were closest to the Company averages in certain respects permits no conclusions as to the effects on the computation of the *differences* from the average in the case of branch offices in other classification codes.

The reasoning of the Supreme Court in *United States* v. *Borden Co.*, 370 U.S. 460, 468–69 (1962), a decision rejecting a cost justification study, is applicable here.

> *But this is not to say that price differentials can be justified on the basis of arbitrary classifications or even classifications which are representative of a numerical majority of the individual members.* At some point practical considerations shade into a circumvention of the proviso. A balance is struck by the use of classes for cost justification which are composed of members of such self-sameness as to make the averaging of the cost of dealing with the group a valid and reasonable indicium of the cost of dealing with any specific group member. *High on the list of "musts" in the use of the average cost of customer groupings* under the proviso of § 2(a) *is a close resemblance of the individual members of each group on the essential point or points which determine the costs considered.* (emphasis supplied).

No convincing showing on this point has been made. [254]

Also significantly detracting from the confidence to be placed in the study is the fact that, of the two basic calculations pertaining to monthly bonus contribution on which Andersen based its conclusion as to the reasonableness of the reporting standard, one, after cross-examination, had to be retracted and the other recomputed.

The product cost and effort studies on which the Andersen evaluation rests were designed to study simply how much it cost to do the reports the way they were being done as a prerequisite to setting prices. There was no attempt in the study to evaluate the quality of the work (Finding 492). The analysis has little relevance, therefore, to the question of whether the procedures are such as to assure maximum possible accuracy.

In view of the foregoing considerations, RX 566 does not outweigh the testimony of respondent's ex-employees in the Commission's case to the effect that they were unable to comply with respondent's

production requirements in accordance with Company policy within a normal workweek.

Allegations of Failure to Disclose Nature and Substance of Reports (Paragraphs 22–23 of the Complaint)

The complaint alleges in paragraphs 22 and 23 that respondent, in certain instances, has failed to clearly and accurately disclose the nature and substance of all its file information (except medical information) on consumers who have properly identified themselves and requested disclosure.

The record shows that, in anticipation of the FCRA's effective date, respondent promulgated extensive new procedures to implement compliance with those provisions of the Act requiring disclosure to consumers (Findings 524–28). Training sessions at all levels of the corporate structure were conducted to acquaint pertinent employees with the new policies and procedures (Findings 521–23). [255]Respondent's disclosure procedures, as set forth in its manuals and other instructional materials, in most instances, provided for compliance with the FCRA provisions.[244] However, the record also shows that respondent's employees did not follow the stated procedures in all instances. Departures at the local level from respondent's official procedures and, more important, from the FCRA requirements, justify the imposition of an order to prohibit such violations.

In respondent's Pittsburgh, Lincoln and Wichita branch offices, inquiring consumers were told they could not receive disclosure of their reports (Findings 529–32). One consumer received disclosure only after his lawyer contacted the Retail office (Finding 529); consumers should not have to retain an attorney as a prerequisite to disclosure. Consumer Humble was denied disclosure of a report prepared in her name because the information was "on" her husband (Finding 530).[245] In the instance of consumer Baker, after being told on two occasions that an insurance company authorization was necessary for disclosure, he was bluntly denied disclosure in the Wichita office when he indicated his desire that a third party be present during the disclosure (Finding 531). The same office advised the McCunes, after an investigation had been conducted on Mrs. McCune, that there was no record of an investigation and, later, that

[244] The procedures found to violate FCRA are discussed individually, *infra*.

[245] Respondent's procedures, however well intended, permitting denial of disclosure to one spouse when there was adverse information on the other (Finding 530 n. 192) violated the FCRA to the extent that it was used to deny a consumer information which was prepared and reported in connection with that consumer.

In the case of consumer Humble, it should be noted, that she was denied disclosure, not only of the information regarding her husband, but also information about herself (Finding 530).

all file information was confidential (Finding 532). [256]The Wichita occurrences, particularly when viewed in light of other FCRA violations in that office (Findings 543, 564) indicate that this particular office (from which no rebuttal witness was presented) had little or no regard for the corporate procedures or compliance with FCRA.

Respondent's instructions pertaining to the disclosure of "nature and substance" of file information as specified by the Act appear to provide for compliance with the statute (Finding 539). However, actual implementation in the field resulted in instances of inadequate disclosure. The record shows that in the Wichita, Denver, Dayton, Manchester, Oxon Hill, Phoenix and San Francisco offices, disclosures were made which omitted certain portions of reports altogether (Findings 543–49). In several instances, highly inflammatory information was withheld. There were omissions of adverse drinking information (Finding 543), drug information (Finding 545), adverse employment information (Finding 546), information that a consumer had run off with a truck driver and was regarded as "trying to take" her husband for his money (Finding 547), and the statement that a consumer used his hands in an effeminate manner (Finding 549). Similarly, respondent appears to have paraphrased particular items disclosed to consumers in such a way as to reduce their impact on a listener (Findings 552–54). In the Canton office, a consumer was told her report indicated she had an unstable marriage. In fact, the information reported was that two sources indicated she had a desire for other men and her husband had a desire for other women (Finding 552). In Wilmington, North Carolina, a consumer was told by respondent that his report showed he made it a point to know the benefits to which he was entitled under insurance policies. The report stated the consumer was well-known in the area as being "claims conscious" and had had his insurance cancelled on several occasions due to excessive claims (Finding 554). Disclosure of this nature changed the tenor of the report and gave an entirely different impression from that given respondent's customer which had received the report. [257]The term "nature and substance" is one which inherently invites imprecise and varying definitions. However, it cannot be interpreted so as to permit respondent's field management to pick and choose among items in a report or, through summarization or paraphrasing, to dilute the thrust of a report during disclosure.

Respondent urges that "at most, complaint counsel have shown an insignificant number of isolated violations" where consumers did not receive full disclosure. (RRB 97). However, the violations found cover

a broad geographic area, and show that some of respondent's employees do not regard compliance with the Act or with the corporate procedures as a high priority. The occurrence of such violations of the Company procedures, without remedial action by respondent, demonstrates a lack of adequate supervision by respondent. Since the institution of visual disclosure in 1974, and the further liberalization of respondent's disclosure policies in 1976 (Findings 556–57), it appears that respondent has made changes to further ensure compliance with FCRA's disclosure provisions. However, in light of the past violations, an order prohibiting respondent from failing to comply with Section 609 is needed to assure future compliance with the Act.

In addition to direct refusals of disclosure and inadequate disclosures, respondent discouraged disclosure by imposing conditions. The procedure established by respondent whereby an inquiring consumer signed a consumer interview form which included a waiver clause regarding reinvestigation (Finding 535), violated Section 609 of the FCRA by putting a condition on disclosure not sanctioned by the Act. While the signing of the form was not an absolute prerequisite for disclosure, consumers would not have been aware that it was not mandatory unless they protested signing. The procedure, in effect, functioned as a condition. Consumers not acquainted with the specifics of the Act were, thus, required to meet more than the conditions specified by Section 610 of FCRA in order to obtain disclosure. Utilization of the waiver provision was a companywide procedure, not a local departure from the corporate instructions. Although discontinued in 1974 or 1975, this procedure was widespread, [258]and a prohibition on such practices is warranted.[246]

Complaint counsel contend, as alleged in the complaint, that respondent's practice of revealing the recipients of reports and noninvestigative sources to consumers only on specific request (Finding 540), violates FCRA (CB, pp. 64–65). Respondent's implementation of Section 609, which provides that "upon request", various items are to be disclosed, does not clearly violate the statute. The statutory words "upon request" should not be used as a means to justify requiring words of art to warrant disclosure, but there is no evidence that respondent has so interpreted them. Absent evidence of bad faith on the part of respondent, the procedures relating to disclosure of

[246] By contrast, the imposition by the Wichita branch office of the condition that an insurance authorization be obtained prior to disclosure in connection with one consumer (Finding 537), is not sufficient to warrant a prohibition directed at this particular practice.

recipients and non-investigative sources on request is not found to violate Section 609.[247]

Respondent has stated its position that claim reports and other reports such as business and some property reports are not subject to the disclosure requirements of FCRA (Finding 558; RB 100–105, 111–113).[248] Respondent relies on the fact that such reports are not consumer reports as defined by the Act. However, the Act does not require disclosure of only consumer reports. Section 609 provides in pertinent part that: [259]

> Every consumer reporting agency shall, upon request and proper identification of any consumer, clearly and accurately disclose to the consumer:
>
> (1) The nature and substance of all information (except medical information) in its files on the consumer at the time of the request.

Respondent asserts that Section 609 of the statute must be read in connection with other provisions of the statute. Respondent states that Section 603(a) states that the definitions contained in that section are applicable for the purposes of the title and the "title" is Consumer Credit Reporting. It contends that, accordingly, the Act does not concern itself with business reports. Respondent further asserts that when the definition of "files" contained in Section 603(g) is read in the context of the above, it is apparent that business reports are not included. The argument is not persuasive. Section 603(g) defines "file, when used in connection with information on any consumer" as meaning "all of the information on that consumer recorded and retained by a consumer reporting agency regardless of how the information is stored." The language of Section 609 and Section 603 is clear. It does not limit the disclosure section to consumer reports. Had Congress so intended, it could easily have provided for such limitations. Thus, all information, including information in the reports other than consumer reports, in a consumer reporting agency's files (except medical information) is subject to the disclosure provisions.[249] Respondent's failure to comply

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[247] The record does show that a consumer was denied disclosure regarding recipients of his report after he so requested (Finding 550). This instance shows again departure at the local level from respondent's procedures.

[248] It should be noted that, while there are examples in the record of respondent's not disclosing claim reports (see Finding 559 n. 211), evidence of specific instances is not necessary or relied upon in light of respondent's stated position and policy, which is that such reports need not be disclosed. This clearly demonstrates the violation.

[249] This decision does not reach the situation not presently in issue, of whether claim reports or other non-consumer reports would be subject to the disclosure provisions if a consumer reporting agency were to establish a completely separate organization to prepare and handle these reports. There is evidence that, as of May 1977, respondent's claims operation was established as an "autonomous profit center" (Tr. 16121). However, the record does not contain sufficient evidence to define that term. *E.g.*, it is not clear whether claim and consumer reports are still handled in some instances by the same people or whether the claim operation is entirely separate from the consumer reporting conducted by respondent.

with such provisions in connection with non-consumer reports violates the Act. [260]

Allegations of Failure To Disclose by Telephone and at Suboffices (Paragraphs 24–25 of the Complaint)

Paragraphs 24 and 25 of the complaint allege, essentially that respondent violated Section 610 of FCRA by failing to give disclosure when requested to do so by telephone and by discouraging telephone disclosure.

Section 610 of FCRA states that a consumer reporting agency is required to give telephone disclosure if a consumer has made a written request, with proper identification and the telephone costs are covered by the consumer. Respondent's procedures regarding telephone disclosure, however, did not require, as permitted by FCRA, that a written request be received before telephone disclosure was given. The corporate policy required only that prior to telephone disclosure, the consumer should be properly identified (Finding 560). The instructions, while clearly permitting telephone disclosure, did imply that, in sensitive cases, in-person disclosure was to be encouraged (Finding 561). There is no indication in the instructions that respondent encouraged or condoned its employees telling consumers that telephone disclosure was not available. As in the case of other corporate policies, however, there were departures from such instructions violative of the FCRA. [261]

The record shows that the Denver office, in particular, had the practice of telling consumers who telephoned for disclosure, that disclosure was available only in respondent's office (Finding 563).[250] In addition, in the Rocky Mount, North Carolina and Wichita offices consumers were told to come to the office for disclosure (Finding 564). Also, respondent, through its Brockton, Massachusetts and Lincoln, Nebraska branch offices, advised consumers who requested copies of their reports that copies were not available but that disclosure could be obtained if the consumers came to the office (Finding 566).

Respondent notes that none of the consumer witnesses presented by complaint counsel had filed a written request for telephone disclosure (RPF 945). Respondent further asserts that the FCRA does not place on respondent the obligation to affirmatively advise consumers of their rights under the FCRA (RB, pp. 100, 109). Respondent is under no obligation to affirmatively advise consumers of their rights in order to comply with the Act. However, once

[250] This finding is not vitiated by evidence in the record which shows that some telephone disclosure was given by the Denver office.

respondent undertook to explain the availability of disclosure, there was an obligation to advise correctly and completely. Similarly, when respondent stated to consumers that disclosure could only be obtained by coming to the office, it implied that telephone disclosure was not available and effectively denied consumers the option of seeking and receiving telephone disclosure. The fact that such consumers had not filed a written request does not affect the determination that these practices violated the Act. Respondent could have stated to such consumers that they could not obtain telephone disclosure because they had not filed a written request or until they filed such a request, leaving with the consumer the option of seeking telephone disclosure. [262]It did not choose to do so. Rather, respondent foreclosed the option of telephone disclosure by stating or implying that telephone disclosure was unavailable. To so foreclose telephone disclosure is tantamount to refusing it and violates Section 610 of FCRA.

The complaint alleges that respondent's failure to provide disclosure from suboffices (Finding 568) violates FCRA's disclosure provisions. However, as respondent argues, the suboffices are not staffed to the same extent as branch offices, do not retain file copies of the reports, and are not equipped to handle disclosure. Respondent's decision to provide disclosure primarily from the branch offices appears reasonable in light of the manpower available in suboffices and the filing system maintained. Respondent established procedures to assure that consumers inquiring at suboffices were properly directed to the appropriate branch offices. There is no evidence that respondent, by establishing these procedures, in any way attempted to escape its disclosure responsibilities. If respondent were required to make disclosure from suboffices, either the branch office files would have to be divided with some files dispersed among the suboffices, or duplicate filing systems would have to be established. Additional manpower in the suboffices would also be needed. The FCRA does not put such a burden on consumer reporting agencies. Complaint counsel asserts that respondent should provide disclosure at some seven suboffices which appear to be better staffed than others (CB 68). To require respondent to establish different procedures for different suboffices would impose a burden not contemplated by the FCRA. Moreover, with telephone disclosure available, consumers will be in a position to avoid traveling great distances for disclosure. [263]

Allegations of Failure To Comply with Section 611 of FCRA (Paragraphs 26–27 of the Complaint)

Paragraphs 26 and 27 of the complaint allege essentially that respondent has violated Section 611 of FCRA by failing to reinvestigate disputed information, failing to record the current status of disputed information and to promptly delete information which can no longer be verified, failing to disclose to the consumer his right to request that respondent furnish notification that a previously reported item has been deleted or that respondent furnish a statement prepared by the consumer to recipients of previous reports, and failing to provide notification to recipients of previous reports when specifically requested to do so by the consumer.

Section 611 of FCRA provides basically that, if a consumer disputes the completeness or accuracy of his report, the consumer reporting agency must conduct a reinvestigation of the disputed information. If the reinvestigation does not confirm the original report, a deletion is to be made in the report. If the original information is confirmed by the reinvestigation, the consumer is entitled to submit a statement setting forth his position, which is to be included with the information in question in any subsequent reports. Notification of any deletions made or consumer statements submitted is to be sent at the consumer's request to parties who have received the report in question (within 2 years for employment reports and 6 months for other consumer reports). The consumer reporting agency has the duty to clearly and conspicuously disclose to the consumer his right to make such a request.

Respondent devised extensive procedures in connection with Section 611 and in good faith attempted to provide for compliance with that section of FCRA (see Findings 574–76). However, Section 611 has been violated at the local level. [264]

The record shows instances in respondent's Baltimore, Boise, Albuquerque, Cleveland and Seattle offices where reinvestigations were not conducted after consumers disputed their reports (Findings 578–82). One consumer disputed highly inflammatory information in her report, yet no reinvestigation was conducted (Finding 578). Respondent offered testimony from the branch office showing the usual procedure followed. However, no attempt to specifically rebut or explain this consumer's testimony was made (see RPF 971i)

In the case of another consumer, respondent implies that because the consumer would not go over his report item by item noting his disputes as to particular items, no reinvestigation was required (see RPF 969d; RB 109). However, the record shows clearly that the consumer disputed the report (Finding 579). The Act requires a reinvestigation when such a dispute is conveyed to the agency. In the case of this consumer, no item-by-item discussion was necessary to

make known the dispute. While it might have been helpful to respondent to know the consumer's exact position on each and every item in the report, his statements throughout the disclosure were adequate to convey a dispute to trigger the statute's requirement that there be a reinvestigation.

With regard to consumer Kasdorf (Finding 580), respondent contends that the consumer did not dispute any significant information in the report (RPF 969c). However, the branch manager of the office testified that dispute as to one's being a "slow payer" was significant but that in this case, the consumer agreed with information in the file (Tr. 11861).[251] The [265]statute requires a reinvestigation when a consumer disputes the "completeness or accuracy" of any item of information. The consumer need not assert there is no truth in an item as reported, but merely that it is incomplete in order to warrant a reinvestigation.

In the case of two consumers (Findings 581–82), respondent contends that there was statutory compliance though no reinvestigation was conducted (RPF 970). These consumers disputed information disclosed to them and indicated they desired further handling of their reports.[252] However, no reinvestigations were conducted. Respondent asserts that, by communicating the disputes to the recipient insurance companies, statutory compliance was obtained. This contention fails for two reasons: the communications sent to the insurance companies in both instances did not set forth completely and accurately the extent of the disputes (see Findings 581–82). More important, however, is the fact that the statute does not give a consumer reporting agency a choice of *either* reinvestigating, *or* sending a statement of dispute to the insurance company, even if such statement accurately describes the consumer's position. The statute clearly calls for a reinvestigation when items are disputed. This requirement could be carried to its logical, yet unworkable conclusion; *e.g.,* requiring a company to conduct a reinvestigation when a consumer disputes his birthdate by a few days. Respondent's procedures permit acceptance of a consumer's version on certain matters without a reinvestigation (Finding 574). In such cases, the statute is not violated; there is no longer any dispute between the consumer and the report. However, if such a procedure is followed, it is essential that the communication to the insurance company (or

[251] The consumer report had stated that Mr. Kasdorf was considered slow in paying bills in Peoria, that he left owing rent and was delinquent in paying an oil company bill (CX 138A). Mr. Kasdorf disputed that he was a slow payer, and that he had left owing rent. He did not dispute the oil company delinquency, but explained that it was paid after being owed for 1 1/2 months (RX 440E).

[252] One consumer gave respondent the names of three people to contact (Finding 581) and the other who was not told that reinvestigation was possible, told respondent she would follow up researching the information herself (Finding 582).

other recipient) set forth clearly that the new information [266]is accepted as true. Otherwise, the recipient company is left with the original information and a denial from the consumer. As a practical matter, the dispute is left unresolved.[253] Absent a full endorsement of the consumer's statement, a reinvestigation is warranted. If respondent chooses not to reinvestigate, and to accept the consumer's statement, then the consumer should be in at least as good a position as if a reinvestigation had confirmed his position.[254]

The record shows also that the Fresno office advised a consumer wrongfully that there was a $5.00 charge for a reinvestigation to be made (Finding 585). The consumer had disputed the report within 30 days of an insurance denial based on the report. Such charge was not authorized by FCRA. The record does not contain evidence sufficient to find that respondent had a practice of imposing unlawful charges as a prerequisite to reinvestigation. Therefore, no specific provision is included in the Order directed to this practice. However, this is another example of failure at the local level to adhere to the Company policies necessary to implement compliance with the Act.

There is evidence in the record showing that, in two instances, respondent failed or constructively failed to promptly delete the information which was not verified in a reinvestigation (Findings 583, 586). In the case of one consumer, the recipient company received from Retail a report stating that the consumer lived with a man, a confirmation of that information, and a letter stating [267] that the consumer disputed the statement and no one would "even admit knowledge of any friends or acquaintances of" the consumer (Finding 586). In fact, at least one person with whom respondent talked, had confirmed the consumer's denial. The communication from Retail, in effect, nullified the deletion of the information from the report. It was constructive failure to comply with Section 611. In the case of the other consumer, respondent's failure to delete health information which the consumer disputed after a reinvestigation in which respondent was "[u]nable to develop further health history" violated the Act (Finding 583). However, the two instances, without more, are insufficient to support an order on this point.

In addition, there is not sufficient evidence in the record to support the complaint allegations that respondent failed to disclose to consumers their right to have notifications sent to recipient compa-

[253] *E.g.*, if Retail chose to accept Mr. Wisniewski's consumer statement that he did not peel rubber, it should have advised the insurance company that it had been learned that Mr. Wisniewski did not peel rubber.

[254] In the case of consumer Van Sickle, respondent followed its procedure of sending a consumer statement rather than reinvestigating. While respondent did not expressly adopt the consumer's statement in the manner set forth above, considering the attendant circumstances, there is no indication that the recipient company would question the correction. All that was involved in the consumer's statement was an explanation and elaboration of the consumer's wife's prior statement regarding the date of an accident.

nies, or failed to provide notifications when requested by consumers to do so.

It should be noted in connection with consumer Spillane, whose experience does not form the basis for a finding of violation (pp. 297–98), that complaint counsel contend that consumers cannot waive their reinvestigation rights under the statute (CB, pp. 127–132).[255] [268]This contention is based on a line of cases dealing with the unavailability of waiver of private rights granted in the public interest. It appears, however, that while the FCRA generally seeks accuracy in reports in the public interest, Section 611 is designed particularly for the protection of individual consumers. Since the right to reinvestigation is designed to protect individuals, it appears to be one which the individuals intended to be so protected can waive. Section 602(a)4 states that there is a need for consumer reporting agencies to respect the consumer's right to privacy. To categorically state that a consumer cannot say to a consumer reporting agency, "I don't want further investigation" would completely negate the right to privacy. Congressional intent to do so is not present in the Act.

Complaint counsel further contend that were waivers found permissible, consumer reporting agencies would be allowed to adopt scare tactics to induce waivers, there would be a substantial number of uninformed waivers by consumers confused about their rights, and the issue of waiver would become an issue in every action to enforce Section 611 (CRB 130). However, these dire results do not appear inevitable. Respondent's instructions which contemplated waivers do not appear to be designed to even encourage waivers, much less to coerce them (Finding 574). Apparently, a waiver can only be exercised under respondent's procedures when a consumer states that he wants no reinvestigation and signs a statement to that effect after being told that the Act requires reinvestigation. The possibility of waivers arising out of confusion seems remote. Also, it is unlikely that waivers will become an issue in every proceeding to enforce Section 611; the exercise of a waiver requires affirmative action by the consumer to be effective. [269]

Allegations Concerning Interchange of Information between Claim and Consumer Reports (Paragraphs 28–29 of the Complaint)

Complaint counsel contend that respondent's claim reports should

[255] It should be noted that, in Mr. Spillane's case, even if waiver were not permitted, there would be no violation. Respondent had already reinvestigated Mr. Spillane's report at the time of the "waiver." Since the Act only requires one reinvestigation, respondent's failure to reinvestigate a second time, particularly when the consumer indicated he desired there be no further reinvestigation, would not have violated the Act.

be considered consumer reports for purposes of FCRA, and that respondent has violated FCRA by failing to adhere to its procedures applicable to consumer reports in the case of claim reports (CB 76–77). Complaint counsel bases this contention, not on an assertion that claim reports are consumer reports *per se,* but rather on respondent's use of its reports. The record shows that respondent has used information from its claim reports in subsequent preparation of consumer reports (Finding 591). In addition, the record demonstrates similar use of consumer reports in subsequent claim reports (Finding 593). Complaint counsel contend that such use transformed claim reports into consumer reports for two reasons: first, claim information could be, and was expected to be, later used in consumer reports. Complaint counsel contend that claim reports, therefore, were "used or expected to be used or collected in whole or in part" for the same purposes as the subsequent consumer reports. The second reason advanced by complaint counsel is that claim reports containing information derived from consumer reports are, in essence, consumer reports. Complaint counsel's argument is not persuasive.

Claim reports from which information is taken for use in consumer reports do not have to be transformed into consumer reports before the protection of the Act applies. Complaint counsel apparently concede, the Act does not regulate the preparation and use of claim reports as such. However, when respondent uses information from a claim report in a later consumer report, respondent must meet the requirements of FCRA in connection with that consumer report, as in the case of all other consumer reports. Information in a consumer report, including that acquired from a claim report, is subject to the disclosure and reinvestigation provisions. The prior status of such information as part of a claim report does not shield it from disclosure and reinvestigation when it [270] has been incorporated in a consumer report. Nor does its later status as consumer report information impose the FCRA requirements on the claim report from which it was taken. Subjects of consumer reports containing claim information should be afforded no less and no more protection than that given in the case of other consumer reports. Thus, no order prohibiting respondent from using claim information in consumer reports is appropriate.[256]

The statute does impose restrictions on respondent's use of consumer report information. Section 604 delineates the purposes for which consumer reports may be used. The statute does not list

[256] If complaint counsel's position were accepted, Section 604 of the statute would become meaningless. As respondent points out (RRB 117), if claim reports were considered consumer reports, respondent would violate Section 604 by furnishing these reports to its customers for use in connection with claims, since this is not a permissible purpose for furnishing consumer reports.

among the permissible uses, utilization of such information in claim reports. Respondent's use of consumer report information in subsequent claim reports violated the statute.

This practice was extensive and did not cease until the recent separation of files. An order prohibiting such use of consumer report information in claim reports is warranted and will issue.

Remedy (Paragraphs 22–29 of the Complaint)

The provisions of the proposed order pertaining to the allegations under paragraphs 22–29 have been modified. Certain provisions of the proposed order have been combined and consolidated to avoid confusion and repetition. The Order issued prohibits respondent from misrepresenting to consumers their rights to disclosure under the FCRA and requires that when a consumer makes an inquiry in connection with disclosure, respondent must advise the [271]consumer of his options regarding disclosure. The Act does not require affirmative disclosure. However, a requirement for affirmative disclosure to consumers is needed in light of respondent's past record of inaccurately and incompletely advising consumers regarding their rights. The Order further prohibits respondent from failing to give disclosure, in person or by telephone, when consumers meet the conditions under FCRA and from failing, while purporting to give disclosure, to disclose the nature and substance of the pertinent file. The words "including claims information" have been deleted from complaint counsel's proposed order. This deletion was made because specifying claim reports without mentioning all types of non-consumer reports could be confusing. The provision as written covers all file information other than medical information. No provision of the Order is specifically directed to the disclosure of recipients or sources of the reports because the record did not show a pattern of withholding such information.

In addition, no provision is included to prohibit respondent from "discouraging" telephone disclosure. The record shows that it is respondent's position that disclosure of certain reports can be handled more effectively by in-person contact (Finding 561). The record also shows that respondent has failed to advise consumers properly of the option of telephone disclosure. The Order requires that respondent advise consumers of their right to telephone disclosure. If respondent properly advises a consumer of the alternative of the telephone disclosure, respondent should be permitted to advise the consumer that respondent feels in-person disclosure is more effective.

Complaint counsel propose in its order, a requirement that

respondent provide inquiring consumers with copies of their reports. The Act does not make such a requirement. Further, respondent has voluntarily changed its disclosure procedures and now provides copies of reports to consumers. The requested provision is unnecessary. [272]

Provisions from the proposed order requiring suboffice disclosure have been deleted as have provisions requiring respondent to advise consumers of the location of their files. Failing to provide disclosure at suboffices does not violate the Act, and the record does not contain sufficient evidence to warrant a provision requiring notification of file location to consumers.

The provision of the proposed order requiring respondent to advise its customers of the address of the branch office preparing reports for the customer has been deleted. Complaint counsel offer no justification for this provision and there is not sufficient evidence demonstrating its necessity.

The provisions of the proposed order relevant to reinvestigation,[257] have also been modified. The time limitation for reinvestigations has been changed from "five working days" to "a reasonable period of time" in accordance with the statute's requirements. The record does not show a pattern on respondent's part of delaying reinvestigations. In addition, the Order does not contain complaint counsel's suggested provision requiring respondent to notify consumers that their reinvestigations have been completed. The provisions of the Order dealing with consumer disclosure apply to disclosure of reinvestigation results. The record does not contain evidence showing a pattern by respondent of singling out and withholding reinvestigation results, or indicating to consumers that disclosure of reinvestigation results cannot be obtained. To require respondent to contact each consumer after a reinvestigation would constitute a burden not warranted in light of the evidence and the assumption that consumers interested in the results of a reinvestigation will contact respondent to obtain this information. [273]

Other provisions in the proposed order pertaining to reinvestigation have been deleted. These relate to the alleged failure to delete information, note the consumer's dispute in subsequent reports, and advise consumers of their right to have report recipients notified of amendments in the reports. There is insufficient evidence to justify such provisions.

Scope of Order

[257] Paragraphs 26 and 27 of the complaint.

Respondent, objecting to introductory language in the proposed order at CB App. C, p. 1, urges the proposed order is too broad. The order, as recommended by complaint counsel, would cover "consumer reports, investigative consumer reports, claims reports or other reports containing information about consumers." Respondent contends that, if any order issues, its coverage should be limited to the type of reporting services formerly performed by Retail Credit Company and now performed by Equifax Services Inc. Respondent states there is no evidence in this record concerning its credit bureaus and no justification for including them in the order (RRB 10).

Commission orders need not be limited to the products involved in the violations demonstrated by the record. The Commission is not confined to prohibiting the identical practices which demonstrated a law violation. It has authority to prohibit acts of the same type or class as committed in the past. *Maryland Baking Co.* v. *FTC,* 243 F.2d 716, 718 (4th Cir. 1957); *Moog Industries, Inc.* v. *FTC,* 238 F.2d 43, 52 (8th Cir. 1956), *aff'd,* 355 U.S. 411 (1958); *Niresk Industries, Inc.* v. *FTC,* 278 F.2d 337, 342–43 (7th Cir. 1960); *Hershey Chocolate Corp.* v. *FTC,* 121 F.2d 968, 971 (3rd Cir. 1941). To be of value, the order must prescribe the method of unfair competition as well as the specific acts by which it has been manifested. *Hershey Chocolate Corp.* v. *FTC, supra.* The Commission, moreover, has wide discretion in determining the type of order necessary to eliminate the unfair or deceptive trade practices found to exist provided that the remedy selected is reasonably related to the violations of law shown. *Jacob Siegel Co.* v. *FTC,* 327 U.S. 608, 612–13 (1946); *FTC* v. *National Lead Co.,* 352 U.S. 419, 428 (1957). [274]

The propriety of the product coverage in an order, however, depends on the facts and circumstances of the particular case. *Carter Products Inc.* v. *FTC,* 323 F.2d 523, 532 (5th Cir. 1963); *The Quaker Oats Co.,* 60 F.T.C. 798, 807–08 (1962); *Royal Crown Cola Co.,* 63 F.T.C. 1950, 1963 (1963); *United Biscuit Co. of America,* 64 F.T.C. 586, 625–26 (1964), *aff'd,* 350 F.2d 615 (7th Cir. 1965), *cert. denied,* 383 U.S. 926 (1966). As previously noted by this agency:

> The reason for the Commission's reference to the facts in each case is simple. The purpose of an order is to prevent statutory violations, the occurrence of which in the future appears likely on the basis of reasonable inference from events that have already taken place . . . .

Transogram Co. Inc., 61 F.T.C. 629, 701 (1962).

In this case, the violations demonstrated by the record must be considered in the context of such factors as respondent's organiza-

tion, structure, compensation system, the nature of the services offered, job demands on employees, etc. On points such as these, the record includes no evidence pertaining to respondent's credit bureaus. Accordingly, no finding can be made on the basis of this record that an order covering the practices of respondent's credit bureaus would be reasonably related to the law violations found herein. The introductory paragraph of the Order will be modified by excluding from coverage those credit reports prepared by Credit Bureau, Inc. of Georgia, Credit Bureau of Montreal and Credit Marketing Services (see RPF 6). [275]

Conclusions

1. The Federal Trade Commission has jurisdiction of the subject matter in this proceeding and of the respondent Equifax Inc.
2. This proceeding is in the public interest.
3. The aforesaid acts and practices of respondent as herein found under Count I of the complaint, were and are to the prejudice and injury of the public and constituted, and now constitute, unfair and deceptive acts and practices and unfair methods of competition, in commerce, within the intent and meaning of the Federal Trade Commission Act.
4. The aforesaid acts and practices of respondent, as herein found under Count II of the complaint, were and are to the prejudice and injury of the public and constituted, and now constitute, violations of the Fair Credit Reporting Act. [276]

Order

I

It is ordered, That respondent, Equifax Inc., a corporation, its successors and assigns, and its officers, agents, representatives and employees, directly or through any corporation, subsidiary, division or other device, in connection with the preparation, offering for sale, sale or distribution of consumer reports, investigative consumer reports, claims reports, or other reports containing information about consumers (except credit reports prepared by Credit Bureau, Inc. of Georgia, Credit Bureau of Montreal and Credit Marketing Services), in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from:

A. Representing, directly or by implication, during the preparation of any report that its investigative personnel are agents or

employees of the company to which the consumer who is the subject of the report has applied for a benefit. [277]

B. Misrepresenting, directly or by implication, that its reports are compiled from information obtained through:

1. in-person interviews with the consumer who is the subject of the report, or the subject's friends, neighbors, or associates;
2. direct observation of the home, neighborhood or other physical surroundings of the consumer who is the subject of the report;

C. Failing to indicate on the copy of the consumer report or consumer investigative report going to respondent's customer that an interview has been conducted on the telephone if that is the fact, unless the service provided is sold exclusively as a telephone service. [278]

II

It is ordered, That respondent Equifax Inc., a corporation, its successor and assigns, and its officers, agents, representatives, and employees, directly or through any corporation, subsidiary, division or other device, in connection with the preparation, offering for sale, sale or distribution of "consumer reports" or "investigative consumer reports," as defined in Section 603(d) and (e) of the Fair Credit Reporting Act, Pub. Law 91-508, 15 U.S.C. 1601, *et seq.,* ("the Act") (except credit reports prepared by Credit Bureau, Inc. of Georgia, Credit Bureau of Montreal and Credit Marketing Services) do forthwith cease and desist from:

A. Submitting consumer report information to persons who it has no reason to believe intend to use the information for a permissible purpose as set out in Section 604 of the Act.

B. Furnishing consumer report information to any person who has not specifically requested such information from respondent with respect to each consumer reported upon. [279]

C. Using consumer report information in any manner, including as reference information or as a lead, in the preparation of any report other than a consumer report.

D. Including any notice or other statement in a consumer report indicating directly or indirectly the existence of items of adverse information which antedate the report by more than the applicable period of time specified in Section 605 of the Act; or otherwise reporting, directly or indirectly, adverse consumer report information or the existence of such information which antedates the report

by more than the applicable period of time specified in Section 605 of the Act.

E. Compelling or inducing its investigative personnel to complete or prepare a certain proportion of consumer reports or investigative consumer reports containing adverse information about or relating to the consumers who are subjects of such reports by utilizing [280] quality audits or any similar system, plan, or procedures.

F. Utilizing any system of quality audits or any similar plan or procedure whereby the performance of branch offices, regions, or other organizational units, with respect to the production of adverse (protective/declinable) information is ranked against companywide or regional averages:

1. unless respondent can demonstrate that such averages constitute a valid standard of comparison for all of the units to which they are to be applied; and

2. unless respondent can demonstrate that the particular survey utilized includes a representative or statistically valid sampling of the branch office or other unit audited or surveyed. [281]

It is further ordered, That respondent shall:

G. Semi-annually conduct unannounced performance reviews of its field representatives, on a random sampling basis acceptable to the Federal Trade Commission, to check the accuracy of their reports, to determine whether the sources listed have been interviewed, whether the sources contacted are logical sources, and whether the information received has been accurately recorded.

H. Submit to the Federal Trade Commission, the results of such performance reviews.

I. Complete the following form for each source of adverse (protective/declinable) information contained in an investigative consumer report. The forms shall be initialed by the investigator preparing the report and forwarded with the report to the recipient. A copy of each form shall be retained in and become part of the consumer's file, as "file" is defined in Section 603(g) of the Fair Credit Reporting Act. [282]

SOURCE INFORMATION ANALYSIS

Adverse (protective/declinable) Information

Covering _____

[Identify adverse information]

was obtained from _____

[Identify source: Employer, neighbor, friend, observation of environment, etc.]

The source gained his [her] information from:

[ ] Personal knowledge;

[ ] Personal observation;

[ ] Hearsay.

The investigator obtained this information through:

[ ] Direct, personal interview;

[ ] Telephone interview;

[ ] Direct, personal observation;

[ ] File information.

It is further ordered, That respondent shall cease and desist from:

J. Misrepresenting to any consumer who requests information concerning himself in respondent's files, the consumer's rights under §609 and §610 of the Act. [283]

K. Failing to inform a consumer who makes a request within the scope of the preceding paragraph:

1. that such consumer has the right to disclosure of such information upon proper identification, by telephone if he pays any toll charge, or in person, at his option; and

2. what constitutes proper identification and to supply or mail, at the consumer's option, all forms which he must execute in connection with the requirements of Section 610 of the Act, to receive disclosure to which he is entitled under the Act and this Order.

L. Failing to give disclosure required by §609 of the Act to any consumer who has contacted respondent and has provided proper identification as required by respondent under §610 of the Act, and [284]has paid or accepted any charges which may be imposed upon him under §612 of the Act.

M. Failing, when giving consumers disclosure, to disclose the nature and substance of all information (excluding medical information) in its files on the consumer at the time of the request.

N. Requiring a consumer as a prerequisite to disclosing information from the consumer's file pursuant to §609 of the Act to fill out or sign a form which authorizes respondent to conduct a reinvestigation of any item the consumer may dispute or to transmit the results of

such reinvestigation to persons to whom it has previously reported the disputed information or which authorizes any business, organization, professional person or anyone else to give full information and records about said consumer to respondent; or interposing [285]any other similar condition or requirement which exceeds those specified in §610 of the Act.

O. Failing within a reasonable period of time to reinvestigate any item of information, the completeness or accuracy of which is disputed by the consumer unless it has reasonable grounds to believe the dispute is frivolous or irrelevant, as required by §611(a) of the Act.

It is further ordered, That respondent herein shall deliver a copy of this Order to cease and desist to all present and future personnel, including employees and representatives, engaged in the preparation of reports, including consumer reports, investigative consumer reports, and claims reports and engaged in the disclosure and reinvestigation of all information in said reports.

It is further ordered, That respondent corporation shall forthwith distribute a copy of this Order to each of its operating divisions. [286]

It is further ordered, That respondent notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondent such as dissolution, assignment, or sale resulting in the emergence of a successor corporation, the creation or dissolution of which may affect compliance obligations arising out of the Order.

It is further ordered, That respondent herein shall within sixty (60) days after service upon it of this Order, file with the Commission a report in writing setting forth in detail the manner and form in which it has complied with this Order. [287]

Appendix A

Evidentiary Conflicts, Credibility and Related Problems

1. Ex-employee Witnesses

The parties' contentions as to the credibility of the Government's ex-employee witnesses have been reviewed. The testimony that certain ex-employees could not complete the workload assigned within a normal workday or workweek is found credible. The testimony of these witnesses with respect to the shortcuts they took to complete cases is persuasive. It is unlikely that they would give such testimony unless it were true. It is improbable that witnesses,

who did take shortcuts such as falsifying sources, would do so unless they could not cope with the workload, since such practices were a firing offense. Moreover, this testimony pertaining to a cross section of respondent's offices, located from coast to coast, is generally consistent on these points.

The testimony of these witnesses has also been weighed against the opinion testimony of rebuttal witnesses that such ex-employees should have been able to do the job without difficulty. The testimony of the Commission witnesses is accepted on this point. The ability to complete a certain number of reports in a given period of time is governed by many variables. These witnesses were in the best position to testify with respect to the specifics of their own situations and they best knew their own limitations.

Respondent contends that the testimony of three ex-employee witnesses is inherently incredible and that no findings whatsoever should be made on the basis of these witnesses. In the case of one witness, no findings will be made in view of his hostility to respondent expressed while testifying (Tr. 1124). In the case of a field representative who worked in the Newark office, respondent's contentions in RPF 97(d) have been considered. It is unlikely his testimony as to the shortcuts he took would be untrue, and findings are based thereon. Respondent adduced considerable evidence to cast doubt on the reliability of a third witness, a former supervisor [288] in the Wayne-Dearborn office. The most damaging appear to be those findings proposed implying he falsified mileage on his expense statements (RPF, pp. 105–106). Such conduct, if proven, is a firing offense (RX 102D). In fact, the witness was not fired but promoted to another office[258] (Tr. 10215–16). Under the circumstances, there are no grounds for ignoring his testimony in its entirety as respondent contends.

2. Documentary Evidence

Findings have been made on the basis of contemporaneous documents from respondent's files. There has been considerable testimony explaining such documents. In some instances, after weighing the inferences to be drawn from the documents against such testimony, findings at variance with the explanations have been made. The finder of fact is entitled to weigh such inferences from contemporaneous documents against subsequent explanations. Cf. *U.S.* v. *Gypsum,* 333 U.S. 364, 395–96 (1948).

[258] Respondent's rebuttal witness testifying on this point concurred with the Regional Vice President on the promotion (Tr. 10215–16).

3. Consumer Witnesses

Complaint counsel presented approximately 60 consumer witnesses who testified regarding alleged violations by Retail. In most cases, respondent offered rebuttal witnesses to the consumers' testimony; and, in many instances, the testimony of the rebuttal witnesses directly conflicted with that of the consumers as to what actually occurred in the various transactions. Thus, the issue of credibility was pervasive in considering the evidence presented by the consumer witnesses. The testimony of some witnesses was accepted as accurately portraying the events related, when rebutted by witnesses who could not recall the incidents in question and testified only [289]regarding the usual procedures in such instances. The recollections of other witnesses were accepted as accurate, even after direct rebuttal or despite inconsistencies not bearing on the particular violation under consideration. Explanation of such credibility findings accompany the findings of fact made in connection with these witnesses. In some instances, despite rebuttal testimony, the essential points involving the violation were not in dispute. Some consumers' testimony was found to be persuasively rebutted by testimony or documents, or not sufficiently clear to support a finding of violation. In other cases, the testimony did not set forth facts which would establish a violation or was offered under paragraphs of the complaint to which it did not relate. Below is set forth, by complaint paragraphs, explanation of the determinations made in connection with certain of these witnesses.

(a) Paragraphs 5-6 of the Complaint

The testimony of consumers Frazzano,[259] Stanley,[260] [290]Moss,[261] Harris,[262] and Baldwin[263] did not set forth facts showing a violation. The testimony of consumers Pierce,[264] Van Sickle,[265] [291]and J.

[259] L. Frazzano's testimony makes it clear that there was no misrepresentation of identity when he was contacted by a Retail employee. Mr. Frazzano testified that the field representative who called him refused to give the identity of her employer and, therefore, he refused to answer her questions (Tr. 3605).

[260] Mr. Stanley testified that the field representative, Mr. Nelson, who interviewed him, did not state that he worked for Retail Credit. However, he also testified that he had known Mr. Nelson for 15 years and knew where he worked (Tr. 217-18). Mr. Stanley had recently acquired an automobile insurance policy (Tr. 216-17). When Mr. Nelson visited him and asked questions regarding his automobiles and their usage, Mr. Stanley "assumed the possibility" that Mr. Nelson was preparing a report (Tr. 258).

[261] There was insufficient evidence to connect Retail to Mr. Moss' experiences with an investigator who visisted him. Thus, his testimony does not support a finding of violation (see RPF 135a).

[262] Mrs. Harris testified that the Retail representative who contacted her stated that he represented Retail Credit (Tr. 1137).

[263] Ms. Baldwin testified that a field representative who interviewed her "flipped a card at [her] and he fired off his name," and then proceeded to ask her questions (Tr. 4730). This testimony is insufficient to show the field representative misrepresented his identity. The fact that his introduction was given quickly and Ms. Baldwin failed to comprehend it, is not necessarily tantamount to a misrepresentation.

[264] Mr. Pierce's testimony contained several statements which tend to cast doubt on his recollections. He stated

(Continued)

Sattler[266] also do not support findings of violation. Considering the direct rebuttal testimony, their testimony is not persuasive.

(b) Paragraphs 22–23 of the Complaint

The testimony of several of complaint counsel's witnesses did not make out a violation under paragraphs 22 and 23 (Parnell,[267] [292] Ptacek,[268] Vail,[269] Roberts,[270] Raber,[271] [293] and Van Sickle.[272]

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that the Retail field representative who visited him in connection with a property report stated that "the sidewalk wouldn't meet his approval" (Tr. 3568). This inherently unlikely statement was denied by the field representative (Tr. 12118–19). In addition, Mr. Pierce stated in connection with a later contact with Retail for disclosure, that Retail told him the computer had made a mistake and he had a bad credit rating (Tr. 3573). Since Retail did not use computers to store information in the pertinent office (Tr. 11898) and the report did not involve credit (CX 222A–B), Mr. Pierce's testimony under this paragraph is not persuasive.

[265] Mrs. Van Sickle's testimony that a Retail field representative who represented she was there in connection with a high school project she was doing (Tr. 3815–16), was effectively rebutted by the credible testimony of the field representative who, at the time of the occurrence would have been 22 years old, that she had never represented herself as a high school student while conducting investigations (Tr. 12277).

[266] Mrs. Sattler's testimony that a Retail field representative visited her after contacting her husband (see Findings 162, 164), and introduced himself as "an insurance inspector" (Tr. 4277) is not persuasive in light of the credible testimony of the rebuttal witness, the field representative. He testified that, after the "first incident" with Mr. Sattler, he made "exceptionally sure" that when he contacted Mrs. Sattler, he introduced himself as Mr. Newman with Retail Credit (Tr. 11745).

[267] Consumer Parnell contacted Retail after hearing from a neighbor that someone had called pursuant to an investigation of him and had made some "inappropriate" comments, *e.g.*, had asked the neighbor if it wasn't a little strange that Dr. Parnell lived with a single man named John. (John was Dr. Parnell's 5-year old son)(Tr. 4323–26). Dr. Parnell's testimony indicates, however, that when he contacted Retail, he was not interested in disclosure and did not request it. He called to advise Retail he would be sending a letter to register his displeasure regarding the manner in which the investigation was conducted, and to find out questions asked (Tr. 4325–27, 4345–46). Dr. Parnell followed up his telephone call with a letter to Retail in which he requested a copy of the questions asked and information obtained (CX 1489A–B). He did not recall having requested a copy in his telephone contact (Tr. 4327), and though he received a written apology from Retail which advised him of the procedure for in-person or telephone disclosure (CX 213), he did not follow up by requesting disclosure (Tr. 4328).

[268] Retail had reported on consumer Ptacek in CX 226A–B, dated January 25, 1972, a motor vehicle report showing traffic violations and in CX 225A–B, dated February 2, 1972, an automobile report which contained more personal information. When consumer Ptacek was told by his insurance agent that the cancellation of his automobile insurance was based on particular items of a personal nature reported by Retail Credit, he contacted Retail for disclosure (Tr. 3546–47). CX 226 was disclosed to him, but CX 225 (which contained the information mentioned by the insurance agent, was not)(Tr. 3547). However, Mr. Green, who conducted the disclosure credibly testified that the reason he did not disclose CX 225 was that it was not in Mr. Ptacek's file (Tr. 12163–64). In fact, CX 225 was never located in the office (Tr. 12173). He explained that about 1 to 2 percent of files are lost or misplaced due to human error (Tr. 12161–62, 12165). Since Mr. Ptacek did not advise Mr. Green that he expected other information, Mr. Green did not suspect the file was incomplete and thus, did not take the steps he would ordinarily take to locate a missing file (Tr. 3550, 3553, 12161–62, 12166–67). Under the circumstances, no violation is found.

[269] In the case of consumer Vail, there was no evidence supporting complaint counsel's allegation of failure to disclose (Tr. 2708–09). According to Mr. Vail himself, the disclosure was complete (Tr. 2695–97).

[270] Mr. Roberts' testimony that his disclosure was incomplete (Tr. 3362–64) was considered in conjunction with his testimony that when the disclosure began, he was read information on a "questionnaire basis" (Tr. 3362) which he said was "trivia" in his mind (Tr. 3372). Therefore, he hurried the disclosure, by such tactics as "butting in during his conversation." (Tr. 3372). According to Mr. Roberts, "I was trying to get him to hurry . . . I was still coming on pretty strong over the phone. So, I did get him to hurry." (Tr. 3362). Under these circumstances, no violation is found.

[271] While consumer B. Raber's testimony was offered under paragraphs 22 and 23, it did not set forth any allegations relating to failure to disclose (Tr. 1002–06).

[272] Mr. Van Sickle received a letter from his insurance company denying renewal of his automobile insurance (Tr. 3821). He contacted his agent and the company was advised that the action had been taken because a Retail report indicated he had had an automobile accident "a couple of weeks prior." Mr. Van Sickle contacted Retail to correct this inaccurate information (he had had an accident, but it had occurred 9 months prior (Tr. 3821–22)). The appropriate correction was made (CX 305, 306). Mr. Van Sickle testified that his "prime purpose" in contacting

(Continued)

In the case of consumers Reinhardt and Robinson, the allegations under paragraphs 22 and 23 seem inextricably related to and dominated by those under paragraphs 24 and 25, relating to telephone disclosure. Their testimony did not pertain to allegations of failure to disclose separate from the allegations of failure to give telephone disclosure. Consideration of this testimony regarding disclosure is confined to the allegations under paragraphs 24 and 25.

Several of complaint counsel's witnesses were effectively rebutted by respondent's evidence. In the case of consumers Bitney, Spillane, Kasdorf and Suerth, the alleged omissions during disclosure concerned items of much less importance and of a far more neutral nature than other items in the reports which were disclosed.[273] [294] Considering together the absence of any motive on the part of Retail to withhold the more innocuous items, and the direct rebuttal of the testimony of these witnesses, it seems probable that the items in question were disclosed, and that such disclosure was forgotten by these witnesses. Thus, no findings of violation have been based on the testimony of these witnesses with respect to disclosure.

The testimony of several other witnesses was directly rebutted by contemporaneous documents tending to show that complaint counsel's witnesses were mistaken in their testimony (L. Raber,[274] Carreathers,[275] Drezek,[276] Hillman,[277] [295]Moss,[278] McKeown,[279] and

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Retail was to correct the error. He did not recall whether he asked what other information was in the report (Tr. 3823–25, 3835). In fact, the report, a Streamlined Auto Report, contained little additional information (CX 303). Under these circumstances, the fact that Mr. Van Sickle's birthdate was not disclosed, is not found to be a violation of the Act.

[273] In the case of consumer Suerth, while the alleged omissions were not completely innocuous items (Tr. 1500–02; CX 280A–C), they were far more neutral than the items which were disclosed (see Finding 578). In addition, Ms. Suerth's memory was shown to be hazy on details surrounding the disclosure, *e.g.*, whether disclosure was given by telephone or in person (Tr. 1497, 1520–21, 1526; CX 300A–B).

[274] Consumer L. Raber's testimony that he called Retail's Baltimore office and was denied disclosure until he made clear he knew his rights under FCRA (Tr. 990–94) and that disclosure, when it was given, was incomplete (Tr. 995–96) was not persuasive. Direct rebuttal by the discloser, Mr. Keilbar, and contemporaneous documents indicated that Mr. Raber's memory was hazy, *e.g.*, Mr. Keilbar actually called Mr. Raber (after Mrs. Raber had requested he do so), advised him he could not receive a copy of the report and gave him telephone disclosure (RX 467A; Tr. 7640–42)

[275] Ms. Carreathers' testimony that she received no disclosure and, thus, gave no corrections during disclosure (Tr. 3327–28, 3339) was effectively rebutted by the testimony of Mr. Tilden (the discloser), supported by RX 412A–C. RX 412A–C showed that disclosure was given, and corrections made at the request of Ms. Carreathers (Tr. 11783–86).

[276] Mr. Drezek's testimony that he did not receive disclosure that his report showed (accurately) that his wife had epilepsy (Tr. 4103) was rebutted by RX 498A, showing this fact was disclosed and confirmed.

[277] Consumer Hillman's testimony that she was refused, or received incomplete disclosure (Tr. 2717–19) was effectively rebutted by testimony of two rebuttal witnesses, Mr. Dewing (Tr. 9309) and Mr. Eaton (Tr. 9322–23), supported by RX 493D and E, which showed Ms. Hillman's recollections were inaccurate.

[278] Mr. Moss' recollection of his disclosure (Tr. 3961–64) was found to be inaccurate when rebutted by the testimony of the discloser, Mr. Pettit (Tr. 11650–52) and RX 455F, which contained Mr. Pettit's handwritten notes from the disclosure and showed additional information given by Mr. Moss which related to the items he claimed were not disclosed.

[279] Mrs. McKeown's recollections were shown to be inaccurate, *e.g.*, she testified that certain things were disclosed to her (Tr. 505–06) which were not even in her report (CX 176A–B).

Notaro[280]).

Several of complaint counsel's witnesses, some of whom were rebutted, appeared to be confused and were unable to clearly state the events which occurred in connection with them. It is impossible to ascertain with confidence what actually transpired in these instances and, in some instances, even what was alleged to have transpired. No findings have been based on their testimony (Mumford 1142-75; J. Crouch, R. Crouch;[281] Conger 3769-89; Comerata;[282] [296]Harrington[283]).

(c) Paragraphs 24-25 of the Complaint

Consumer Lowe's testimony (Tr. 2091-103) does not support a finding of violation. She was unable to remember the events in question and did not testify with clarity regarding these matters. Similarly, no findings of violation were based on the testimony of consumer Conger (Tr. 3769-69).

In the instance of consumer Robinson, there was insufficient evidence to link the allegations to which he testified to Retail.[284] Thus, no findings are based on his testimony.

The testimony of consumers Parnell, L. Raber, Hillman, Moss and Phares contained allegations of failure to disclose. While the contacts in these cases took place by telephone, there was no evidence that telephone disclosure was singled out or that the treatment of these consumers was a result of their calling by telephone rather than going to the offices. Thus, the evidence pertaining to these witnesses was considered under paragraphs 22 and 23 under which it was also offered.

Consumers Luster (Tr. 3164-84), B. Raber (Tr. 1002-06) and M. McCune (Tr. 4378-412) were also offered under these paragraphs,

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[280] Mr. Notaro's memory was found to be inaccurate. He appeared to be confused with regard to which of Retail's offices he contacted at various times (see Tr. 4460-61, 10545-47; RX 457A-B). The contemporaneous documents were found to be persuasive.

[281] The testimony of Mr. and Mrs. Crouch conflicted on major issues, *e.g.*, whether disclosure was given (Tr. 3186-88, 3207). The rebuttal witness, the discloser, testified as to yet another recollection (RX 421D, pp. 34-35). Under the circumstances, no findings of violation can be based on their testimony.

[282] In the case of consumer Comerata, her testimony on cross-examination indicated that the most significant item in her report—that Retail was unable to locate anyone in Aspen who knew her—was disclosed (Tr. 3227; CX 63, 64, 65). The testimony was unclear regarding whether anything else was disclosed (Tr. 3219-20).

[283] The introduction of CX 1570A, a consumer log from the Chicago office (Tr. 14841-42), corroborated Mr. Harrington's testimony that he contacted the Chicago office in March of 1973 (Tr. 2515-16) and impeached the testimony of respondent's witness, Mr. Brenner (Tr. 9621). However, the record in connection with Mr. Harrington is confused and he appeared generally unsure of what actually took place. No finding of violation is based on this testimony.

[284] Mr. Robinson testified that he called Retail and was refused disclosure by telephone (Tr. 2175). However, rebuttal testimony indicated that Mr. Robinson may have called a local credit bureau rather than Retail (Tr. 7021-61).

but their testimony contained no facts relevant to telephone disclosure. Thus, no findings are based on their testimony. [297]

The testimony of consumer Drezek regarding telephone disclosure (Tr. 4102) does not support a finding of violation when read in light of the rebuttal testimony and contemporaneous documents which showed that Mr. Drezek did not recall accurately with whom he spoke at Retail and what was told to him (see p. 294 n. 276).

(d) Paragraphs 26–27 of the Complaint

The testimony of Mr. and Mrs. Crouch does not support a finding of violation in connection with reinvestigation as their testimony indicated that they were unable to clearly remember the events in question (see p. 295 n. 281).[285] Similarly, no violation was found in the case of consumer McKeown.[286] In addition, consumer Moss' recollections were found to be confused, and a finding of violation is not based on his testimony (see also p. 295 n. 278).

Consumer Mumford's testimony was too confused to permit a finding of whether disclosure was complete (see p. 295) or the reinvestigation complete. The record does show a reinvestigation was conducted (CX 201, 202A–B, 197, 198A–B). Under the circumstances, no violation is found.

The testimony of consumers Spillane,[287] [298]T. Smith,[288] Van

[285] The item that both Mr. and Mrs. Crouch alleged was disputed, namely, that Mr. Crouch was disabled and incapable of driving (Tr. 3210, 3187–88) was not even in the report in question (CX 74A–C).

[286] Mrs. McKeown testified that she disputed facts disclosed to her (Tr. 505–06, 511–12). However, the alleged dispute concerned information not in the report (CX 176A–B; see also p. 295 n. 279).

[287] Consumer Spillane disputed his report during disclosure (Tr. 3844–47) and supplied Retail with the names of references to be contacted (Tr. 3848). A reinvestigation was conducted, but the references Mr. Spillane provided were apparently not contacted (CX 267; Tr. 3848). Mr. Spillane received disclosure of the results of the reinvestigation (Tr. 3849), and disputed them (CX 265). When it was suggested to Mr. Spillane that he write out his dispute in detail, he responded that he did not want inaccurate information and a denial in the file; he wanted the inaccurate information deleted (Tr. 3851). The discloser also suggested that yet another reinvestigation could be conducted, but Mr. Spillane rejected that alternative, stating he "didn't feel that [his] reputation could stand another one of [their] investigations" (Tr. 3852). Under the circumstances, no violation is found. FCRA imposes no duty to contact a consumer's references in a reinvestigation, nor is there a duty to continue reinvestigating after one reinvestigation has been completed and the consumer declines an offer of further reinvestigation.

[288] As noted earlier (Finding 546), the information which Mr. Smith disputed was deleted from his report and a corrected copy sent to the requesting company. Thus, no failure to reinvestigate is found.

Sickle,[289] Vail,[290] Stanley, [291] [299]Roberts,[292] and Dealy[293] does not set forth facts which show any violation. [300]

Appendix B

Abbreviations used throughout this Initial Decision are as follows:

CX – Complaint counsel's exhibit
RX – Respondent's exhibit
Tr. – Transcript page
CB – Complaint counsel's brief
CPF – Complaint counsel's proposed finding (reply findings of fact)
CRB – Complaint counsel's reply brief
RB – Respondent's brief
RPF – Respondent's proposed finding
RRB – Respondent's reply brief

Opinion of the Commission

By Pertschuk, *Commissioner:*

I. Background

A. The Law

Congress enacted the Fair Credit Reporting Act ("FCRA"), 15 U.S.C. 1681, *et seq.* (1976), in order to ensure that "consumer

[289] In the case of Mr. Van Sickle, the record shows that a notice was sent to the insurance company correcting the item Mr. Van Sickle disputed (CX 305, 306; Tr. 3824-25). There is no evidence in the record to support complaint counsel's speculation that the recipient insurance company regarded this correction notice as self-serving (CPF 1061; see also p. 266, n. 254).

[290] The record shows that a reinvestigation was conducted after Mr. Vail disputed his report and that the results were transmitted to the requesting company with corrections (CX 292, 293, 294A–B, 295, 297A–B, 299A–B).

[291] The record evidence surrounding Mr. Stanley's contact with Retail does not support complaint counsel's position that reinvestigation in this instance was not conducted within a reasonable time (CCB, p. 70; CPF 1006). Mr. Stanley received disclosure on either January 24 or 25, 1972, (RX 495D, G). Retail notified the recipient company of its intention to reinvestigate on January 28, 1972 (RX 495F). On January 31, 1972, the reinvestigation was ordered (RX 495B; CX 271C). This brief delay was explained in a memorandum to the Home Office as being due to the branch office's attempt to locate the report on Mr. Stanley for homeowner's insurance which Mr. Stanley stated was cancelled at the same time as his automobile insurance; it was the automobile report which he disputed (RX 495B). This explanation, on its face, appears reasonable, and no finding of violation is made.

[292] While consumer Roberts' testimony was presented under these paragraphs, his own testimony indicates that, after he disputed information disclosed to him, respondent conducted a reinvestigation which was sent to the insurance company involved (Tr. 3375). In addition, the record contains documentary evidence showing a reinvestigation (CX 1464A–C).

[293] The testimony of consumer Dealy does not support a finding of violation. He testified that, while he disputed information in his file and he was told there would be a reinvestigation, he never was contacted by Retail regarding the results (Tr. 3402). A reinvestigation was conducted (CX 343 O–Q). Complaint counsel's contention that there is a duty to contact the consumer for disclosure of reinvestigation results (Tr. 3403) is rejected.

reporting agencies adopt reasonable procedures for meeting the needs of commerce for consumer credit, personnel, insurance, and other information in a manner which is fair and equitable to the consumer, with regard to the confidentiality, accuracy, relevancy, and proper utilization of such information * * * ." FCRA, 602(b).

To protect the confidentiality of information concerning consumers, the statute permits "consumer reporting agencies"[1] to [2]disclose "consumer reports" only to those who have a legitimate business need for the information.[2] Because Congress recognized [3]that some inaccuracy was inevitable, *see* 115 *Cong. Rec.* 2411 (1969) (remarks of Sen. Proxmire), it chose not to render consumer reporting agencies strictly liable for inaccuracies in a report. Instead, it (1) required the use of "*reasonable* procedures to assure maximum possible accuracy of the information concerning the individual about whom [a] report relates," FCRA, Section 607(b) (emphasis added); (2) prohibited, as a general rule, the communication of obsolete adverse information, that is, most adverse information reported after seven years, FCRA, Section 605; (3) required the updating of information obtained from an investigative consumer report[3] before it could be included in a

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[1] The Act focuses on information contained in a "consumer report," that is, "any written, oral, or other communication of any information by a consumer reporting agency bearing on a consumer's credit worthiness, credit standing, credit capacity, character, general reputation, personal characteristics, or mode of living" and "which is used or expected to be used or collected in whole or in part for the purpose of serving as a factor in establishing the consumer's eligibility for (1) credit or insurance to be used primarily for personal, family or household purposes, or (2) employment purposes, or (3) other purposes authorized under Section 604." [FCRA, 603(d)] Section 603(d) contains several exclusions from the definition, including reports "containing information solely as to transactions or experiences between the consumer and the person making the report * * *."

A "consumer reporting agency" is, in turn, defined as a "person which, for monetary fees, dues, or on a cooperative nonprofit basis, regularly engages in * * * the practice of assembling or evaluating consumer credit information or other information on consumers for the purpose of furnishing consumer reports to third parties, and which uses any means or facility of interstate commerce for the purpose of preparing or furnishing consumer reports." [FCRA, Section 603(f)] The permissible purposes, set forth in Section 604, are quoted in note 2 *infra*.

[2] Section 604 of the FCRA provides as follows:

A consumer reporting agency may furnish a consumer report under the following circumstances and no other:

(1) In response to the order of a court having jurisdiction to issue such an order.

(2) In accordance with the written instructions of the consumer to whom it relates.

(3) To a person which it has reason to believe —

(A) intends to use the information in connection with a credit transaction involving the consumer on whom the information is to be furnished and involving the extension of credit to, or review or collection of an account of, the consumer; or

(B) intends to use the information for employment purposes; or

(C) intends to use the information in connection with the underwriting of insurance involving the consumer; or

(D) intends to use the information in connection with a determination of the consumer's eligibility for a license or other benefit granted by a governmental instrumentality required by law to consider an applicant's financial responsibility or status; or

(E) otherwise has a legitimate business need for the information in connection with a business transaction involving the consumer.

[3] An "investigative consumer report" is a

consumer report or portion thereof in which information on a consumer's character, general reputation, personal characteristics, or mode of living is obtained through personal interviews with neighbors, friends, or associates of the consumer reported on or with others with whom he is acquainted or who may have knowledge concerning any

(Continued)

subsequent consumer report, FCRA, Section 614; and (4) imposed restrictions on the use of public record information. FCRA, Section 613.

Congress also imposed a variety of procedural requirements designed to enable consumers to identify and correct inaccurate information. For example, the users of consumer reports must inform the consumer of the name and address of the consumer reporting agency responsible for preparing a consumer report that was used to deny credit, insurance, or employment or to increase the charge for credit or insurance. FCRA, Section 615(a). Also, the statute requires consumer reporting agencies upon request (and without regard to whether a user of the file has taken adverse action against the consumer) to inform him or her "clearly and accurately" of the "nature and substance" of information in its files on the consumer at the time of the request, the [4]sources of the information,[4] and, with certain limitations, the identity of the recipients of any consumer report on the consumer. FCRA, Sections 609, 610.

If the consumer disputes the completeness or accuracy of any item of information contained in his or her file, the reporting agency must "within a reasonable period of time reinvestigate and record the current status of that information unless it has reasonable grounds to believe that the dispute * * * is frivolous or irrelevant." If the information is found to be inaccurate or can no longer be verified, the agency must promptly delete the information. FCRA, Section 611(a). In case the reinvestigation does not resolve the dispute, the consumer may file a brief statement setting forth the nature of the dispute, FCRA, Section 611(b), and, unless there are reasonable grounds to believe that the statement is "frivolous or irrelevant," the reporting agency, in any subsequent consumer report containing the information in question, must clearly note that it is disputed by the consumer and provide either the consumer's statement or a clear and accurate summary. FCRA, Section 611(c). The statute directs the reporting agency, following deletion of information found to be inaccurate or unverified, or the addition of any notations as to disputed information, to notify previous recipients of the information designated by the consumer that the information has been deleted or to send them the consumer's version of the dispute. FCRA, Section 611(d).

Administrative enforcement of the FCRA is assigned to the

such items of information.

FCRA, Section 603(e).

[4] Except in the course of discovery in an action brought under the FCRA, the consumer reporting agency need not disclose the sources of information acquired solely for use in preparing an investigative consumer report.

Commission, except to the extent that enforcement is specifically committed to other government agencies under Section 621(b). For the purposes of the Commission's exercise of its enforcement responsibilities under the FCRA, a violation of any requirement or prohibition imposed by the statute constitutes an unfair or deceptive act or practice in violation of Section 5 of the FTC Act, 15 U.S.C. 45 (1976). FCRA, Section 621(a).

B. The Respondent

Equifax Inc.[5] is one of the nation's largest consumer reporting agencies.[6] Directly or through its subsidiaries, among [5]other things, it supplies financial and credit reports for use in evaluating the financial reputation and payment history of individuals who seek credit; sells personnel selection reports used to evaluate applicants for employment; supplies insurance companies with information used to determine the desirability of applicants as risks for insurance; and prepares information used to assess claims made against insurers.

Since April 1, 1977, consumer reports, including personnel reports and reports sold to insurance companies for underwriting purposes and claim investigations, have been the responsibility of Equifax Services, Inc., a wholly-owned subsidiary. These reports are prepared in Equifax Services' 219 branch offices and 1000[7] "suboffices." As of May 1974, respondent employed approximately 4600 salaried field representatives to perform the investigative work underlying the reports. (ID 75, 89)[8]

II. Complaint and Initial Decision

The complaint in this case charged Equifax Inc. with a variety of

[5] Respondent was known as Retail Credit Company when the complaint in this case issued. It was renamed Equifax Inc. effective January 1, 1976.

[6] Some of respondent's activities are not those of a "consumer reporting agency" as defined by Section 603(f) of the FCRA.

[7] These numbers of offices are accurate as of April 1976.

[8] The following abbreviations will be used in this opinion:

ID	–	Initial decision finding no.
ID p.	–	Initial decision page no.
Tr.	–	Transcript page no.
CX	–	Complaint counsel's exhibit no.
RX	–	Respondent's exhibit no.
RAB	–	Respondent's appeal brief.
CAB	–	Complaint counsel's appeal brief.
R. Ans.	–	Respondent's answering brief.
C. Ans.	–	Complaint counsel's answering brief.
RRB	–	Respondent's reply brief.
CRB	–	Complaint counsel's reply brief.
RPF	–	Respondent's proposed finding no.
CPF	–	Complaint counsel's proposed finding no.

violations of the Fair Credit Reporting Act and Section 5 of the Federal Trade Commission Act. Violations of the FCRA alleged in the complaint include furnishing information about consumers to persons respondent has no reason to believe intend to use the information for one of the permissible purposes set out in the statute; reporting the existence of obsolete, adverse information; and failing to disclose to consumers, upon request, the nature and substance of information in its files. The complaint also alleged that respondent employs certain procedures which do not assure the maximum possible accuracy of information concerning individuals about whom its reports relate, including a "salary/production [6] system" which "requires or compels" its personnel to prepare an unreasonable number of reports, and quotas which "require or compel" its personnel to prepare a certain proportion of reports containing adverse or derogatory information.

The complaint also charged several violations of Section 5, including misrepresentations to consumers by respondent's investigative personnel that they are agents or employees of the companies to which the consumers have applied for benefits; representations to its customers (those who purchase its reports) that information was gathered in in-person interviews in cases when, in fact, the interviews were conducted by telephone; and employing authorization forms for the release of medical information which misrepresent that the information is being sought for the exclusive use of insurance companies. Finally, the complaint alleged that respondent's investigators have misrepresented to consumers the purposes of those investigations which are designed to evaluate claims for loss or injury under an insurance policy.

After a lengthy trial, Administrative Law Judge ("ALJ") Theodor P. von Brand entered a carefully documented and well-reasoned initial decision sustaining most of the complaint allegations. He found, however, that several were not supported by the record and that two of the alleged violations of Section 5 were immunized by the McCarran-Ferguson Act, 15 U.S.C. 1011, *et seq.* (1976), as the "business of insurance." The case is now before the Commission on cross-appeals filed by complaint counsel and respondent from certain of the ALJ's findings and also from his proposed order.

III. Fair Credit Reporting Act Charges

A. Reasonable Procedures to Assure Maximum Possible Accuracy

In enacting the Fair Credit Reporting Act, Congress' primary

concern was the dissemination of reports containing inaccurate adverse information[9] about consumers. The Senate report declared that "[t]he purpose of the fair credit reporting bill is to prevent consumers from being unjustly damaged because of inaccurate or arbitrary information in a credit report." S. Rep. No. 91-517, 91st Cong., 1st Sess. 1 (1969). Senator Proxmire, upon introducing [7]the Senate bill, stated why he was concerned about even small amounts of inaccurate information in credit reports:

> Perhaps the most serious problem in the credit reporting industry is the problem of inaccurate or misleading information. There have been no definitive studies made of just how accurate is the information in the files of credit reporting agencies. But even if it is 99 percent accurate—and I doubt it is that good—the 1 percent inaccuracy represents over a million people. While the credit industry might be satisfied with a 1-percent error, this is small comfort to the 1 million citizens whose reputations are unjustly maligned.

115 *Cong. Rec.* 2411 (1969).

Similarly, Representative Zablocki, one of the authors of the House bill, expressed his concern about the impact on individuals:

> [W]hen we consider the fact that each time there is an error by an agency, an individual suffers not only embarrassment and inconvenience but financial loss and possibly even the loss of his job, his insurance, and even his mortgage, then we have put the danger of incorrect reports in proper perspective.

Id. at 2517.

Congress, as noted previously, imposed on reporting agencies not strict liability, but an affirmative duty to take reasonable steps to assure that the information in a consumer report is correct. Section 607(b) provides that "[w]henever a consumer reporting agency prepares a consumer report it shall follow reasonable procedures to assure maximum possible accuracy of the information concerning the individual about whom the report relates."

While the legislative history and the statute itself shed little light on the meaning of the words "reasonable procedures to assure maximum possible accuracy," it is clear that Congress intended to mandate something more than the use of some care to avoid inaccurate reporting, and something less than a duty to achieve absolute accuracy or even "maximum possible accuracy" in every report. We construe Section 607(b) to require reporting agencies to do whatever is reasonable under the circumstances to minimize the chances that consumers will be harmed by inaccurate reporting. If

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[9] "Adverse information," as used in this opinion and in the order, means information which may have, or may reasonably be expected to have, an unfavorable bearing on a consumer's eligibility or qualification for credit, insurance, employment, or other benefit, including information which may result, or which may be reasonably expected to result, in a denial of or increased costs for such benefits. (*See* RPF 1(h).)

an agency employs a procedure which does not offer the best assurance of producing the most accurate reports, it ought to have a strong justification for doing so. [8]

With some qualifications, we uphold the judge's findings that respondent has failed to meet this duty.[10]

1. Pressures To Develop Adverse Information

The complaint alleged that respondent has imposed quotas which "require or compel" its investigative personnel to prepare a "certain proportion" of reports containing adverse information. According to the complaint, these alleged quotas "have the tendency and capacity to promote incomplete or inaccurate reports." Because of Congress' concern about the serious damage which the misreporting of adverse information can inflict on consumers, we should be skeptical of any procedure which may induce employees to falsify, unduly emphasize, or exaggerate adverse information.

While the complaint implicitly asserted that quotas for the production of adverse information are inherently incompatible with the rigorous standard prescribed by Section 607(b), the ALJ found unreasonable only the particular system used by respondent. Respondent appeals from Judge von Brand's conclusion that its system was not reasonable, and complaint counsel appeal from the judge's failure to decide that such quotas are inherently unlawful.

The parties agree that respondent has conducted "quality audits" of the reports prepared by its branch offices and that these audits have included measurements of each office's production of "declinable" information (adverse information which might cause an insurance company to decline an underwriting application or to fail to renew an existing policy) and "protective" information (adverse information which might cause an insurer to charge a higher premium). (ID 281–82, 294–95; RPF 754(a), (b))[11] In 1975, respondent altered the audit procedure so as to obtain regional rather than individual office results and, the following year, it stopped auditing protective and declinable information. (ID 297)

Before these changes were implemented, however, branch offices were ranked into upper, middle and lower third positions according [9]to how their current performances in producing protective and declinable information compared with those of all other branch offices during the preceding year. (ID 305) This ranking created

[10] We agree with respondent that complaint counsel had the burden of proving their case by a preponderance of the evidence. *See, e.g., Leonard F. Porter, Inc.*, 88 F.T.C. 546, 627 (1976). Respondent has acknowledged that the ALJ understood complaint counsel's evidence was to be tested by this standard. (Transcript of Oral Argument 16)

[11] Besides measuring protective or declinable information, auditors would attempt to determine whether the reports under review satisfied respondent's standards for completeness and for clerical accuracy

pressure on respondent's employees. The judge found that "[t]here was considerable rivalry among respondent's offices, and everyone wanted to be at the top of the performance category in terms of all phases of branch office performance measured by quality audits, including production of declinable information," although "[s]ometimes a Regional Vice President was satisfied with performance in the middle third." (ID 311 & n.101)

The ALJ determined that, in the quality audits, too few reports were sampled to permit a valid survey of the performance of the individual branch offices (ID 335–36; ID p. 239),[12] and respondent does not challenge that finding. Nor does respondent question the finding that the same percentage of adverse information could not be expected from each office "because of differing geographic as well as economic and social factors." (ID 332)

Respondent does appeal, however, from the ALJ's finding that the quality audits and the subsequent rankings of offices impliedly set quotas for the production of unfavorable information. (ID 343) Respondent describes the audits simply as a training tool designed to improve the quality of its reports and asserts that it did not impose sanctions upon field representatives or "significant" sanctions upon branch office managers who failed to develop adverse information. (RAB 61–62)[13]

We need not decide whether, as the ALJ found, the pressures created by respondent's quality audits may properly be characterized as "quotas," implicit or explicit.[14] The quality audits clearly resulted in the setting of objectives which field representatives [10]were expected to meet in order to assure that their offices would score well in the audits. The audits placed a premium on the production of adverse information and induced employees to prepare reports which contained inaccurate adverse information.

Contrary to respondent's contentions, the record clearly shows that respondent used the audit results for purposes other than simply identifying candidates for additional training. The amount of bonus money received by a branch office manager was based in part on audit performance,[15] and the performance of the field representa-

[12] Some of respondent's own managers, including regional vice presidents, expressed doubts that the audit data were necessarily representative. (ID 331)

[13] Related to this assertion, the judge found that "[t]he record does not demonstrate an overall pattern of overt sanctions such as firings or the withholding of salary increases or promotions as penalties for the failure to achieve specific levels of protective/declinable information." (ID p. 238)

[14] Respondent argues that the audit system could not impliedly have set a quota because the ALJ did not, and could not, state what the quotas are. The record, however, is replete with references to specific objectives which were communicated to respondent's employees. (*E.g.*, ID 319; Tr. 1761–62)

[15] Respondent asserts that

> it is true that performance on home office audits was one factor taken into account in determining a

(Continued)

tive in the quality audits was "one factor among several" considered by the branch managers when they made their salary recommendations. (ID 312–13)

The significance of the quality audits to respondent's managers is indicated by evidence that they took steps to pressure employees to produce enough adverse information to permit their offices to score well in the audits. The manager of one office informed his field representatives that " * * * until such time as each individual met the declinable objective [for two types of reports] * * * there would be no salary increases for any [11]members of the unit." (ID 319(c))[16] Investigative personnel were made aware that they were expected to obtain the specified amounts of protective and declinable information. (*E.g.*, Tr. 1761–62, 1845;[17] ID 319, ID p. 239; *see* RPF 770.) A supervisor in another of respondent's branch offices was placed on probation because of management's judgment that his unit's production of declinable information was too low. (ID 319(h); RX 446B)

Respondent's higher level management brought pressure to bear on lower level management, usually branch managers, to achieve high audit scores (ID 299, 318),[18] and branch managers, [12]in turn,

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manager's bonus (ID at 238), but it was a minor factor that might or might not affect a given bonus (RPF 407–13), and some managers either were not even aware that it was taken into account or considered it an insignificant factor. (RFP [sic] 774c)

RAB 61 n.56. While performance on the quality audits was just one of several factors, we cannot find that it was sufficiently "minor" that it would not induce a manager to attempt to score well on the audits. In any case, the combination of incentives (such as the managers' bonus) and disincentives clearly induced many employees to take the quality audits seriously, and to conclude that they were expected to produce at least the specified amount of protective and declinable information.

Nor can it be very helpful to respondent's case that "*some* managers either were not even aware that it [performance on home office audits] was taken into account or considered it an insignificant factor." (RAB 61 n.56) (emphasis added)

[16] Contrary to respondent (R. Ans. 54), we believe the ALJ properly relied on the memorandum (CX 1283A) cited in the finding despite complaint counsel's failure to call its author as a witness. Because the document speaks for itself, it was not complaint counsel's burden to proffer testimony as to its meaning.

[17] Even though respondent called a number of current and former employees who testified that they were unaware of pressures to produce adverse information, the ALJ was entitled to find that the pressure existed. That not all employees may have been aware of, or affected by, the pressures is not inconsistent with a finding that other employees were pressured to produce the requisite amount of adverse information. Indeed, the documentary evidence cited by the ALJ requires such a finding. (ID 319)

The ALJ found the testimony of these witnesses, and that of most of the other former employees called by complaint counsel, credible as to the shortcuts they took to meet their production quotas. (ID pp. 287–88) We find no basis to accord their testimony less weight on the issues of whether pressures were imposed on them to produce adverse information and the effects of any such pressures on the manner in which they prepared their reports.

We have been presented no persuasive reasons by either complaint counsel or respondent to upset the careful credibility determinations made by the ALJ as to the various witnesses called in this case.

[18] For example, one Regional Vice President told his managers:

> All of us naturally would like to be furnishing customers with a service that ranks above other offices and other regions. All of us would like to be in the top third as we measure an office and region.

CX 1127A.

Another Regional Vice President expressed his dissatisfaction with the performance of one of the branches in his territory:

(Continued)

transmitted that pressure to their field representatives. A rivalry developed among branch offices and among regions to outdo each other in the audits. (ID 311)

In light of these findings, we are not troubled by the absence of an overall pattern of overt sanctions applied to employees who produced "unsatisfactory" amounts of adverse information. Incentives, like sanctions, are designed to influence behavior, and the incentives employed by respondent, together with the more subtle sanctions, impressed upon many field representatives and their supervisors the importance of ranking high in the quality audits.

The ALJ found that the audit procedure had the potential "to adversely influence report writing * * * ." (ID p. 239) The record supports this conclusion. For example, the record includes evidence of the efforts of one manager to teach field representatives to phrase adverse information in a forceful manner. A memorandum written by this branch manager to one of his suboffices urging the omission of qualifying phrases such as "it is believed" and "sources believe" (CX 1565A) was designed to strengthen the impact of the adverse information which was discovered, thus increasing the branch's production of declinable information. (ID 329(b))[19] The goal, according to the manager [13]of the Albuquerque branch office, was to "put the decline across," that is, to transform what would otherwise merely be "protective" information into "declinable" information. (ID 329(a))[20] We agree with the ALJ that when the goal is "maximum possible accuracy," it is not reasonable to discourage the qualification of adverse information the certainty of which is in doubt, and that respondent's quality audits had this impermissible effect.

Additionally, the evidence shows that some management personnel urged lower level managers and field representatives not to

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I know you and your people are going to be disappointed with the Declinable of 5.4% in the second round analysis * * *, *but I also know that the personnel in Albuquerque will immediately set about to make sure the next round analysis will reflect only upper third rankings in all categories!*

CX 772 (emphasis added).

[19] Respondent contends that the point of the memorandum was not to eliminate qualifying information from reports when that qualifying information was needed to make the report accurate (RAB 64–65), but was, instead, simply a product of the manager's view that "if a source stated to a field representative that he was not certain that an individual was involved in an accident, but that he believed he was, that would not be a satisfactory basis for submitting the report." (RAB 64) We reject respondent's construction of the document. The memorandum, while urging elimination of these qualifying phrases, says nothing about omitting from reports information about which the source is uncertain. Moreover, although this communication states that these qualifying phrases "tend to disturb the confidence of the underwriter in our report," a concern which could well be unrelated to an interest in ranking high in an audit, a subsequent memorandum to the Regional Vice President, quoted in ID 329(a), supports the ALJ's inference that the suggested omission of the phrases was designed to increase the office's production of declinable information.

We are, therefore, not persuaded by the testimony that these instructions were simply part of an effort "to provide as concise and accurate [a] report as we could, and our effort was to eliminate unnecessary words and unnecessary phrases." (Tr. 11819)

[20] The ALJ properly was unpersuaded by the explanation offered by the author. (Tr. 11828–29)

report information which would tend to negate derogatory information discovered during the course of an investigation. A Regional Vice President, for the sake of improved audit performance, wrote to a branch office manager that "[o]ne of the biggest problems" contributing to the office's placement in the lower third of all offices in one of the audits

was that when your people would develop declinable information it was worded in such a way that its effectiveness was decreased. These were usually such comments as[:] ["]this is the only known instance known instance of driving while intoxicated["] or that the subject had stopped drinking completely three months ago and was now reformed.
ID 330. [14]

A former field representative testified that, to reach his prescribed level of declinable information, he would attempt to make it appear that an "excessive" drinker drank "a little more than he actually did." Where sources could not report how often the person had been seen drinking, the field representative would fabricate a number. (Tr. 1782)[21]

Despite this evidence, respondent complains that the record does not include any reports in which adverse information was falsified. (RAB 59) However, in view of the testimony and the [15]written instructions cited above, we do not find this shortcoming fatal. The record demonstrates that field representatives, in their effort to meet the objectives inspired by the quality audits, have been instructed, in effect, to misreport adverse information. We recognize that proof that a challenged procedure has consistently yielded reports free of inaccurate adverse information would shake a claim that a procedure is unreasonable. Similarly, proof that its use has resulted in inaccurate reporting would bolster a claim that it is not a "reasonable procedure to assure maximum possible accuracy." *Cf.*

[21] With respect to the credibility of this witness, *see* note 17 *supra.* The testimony of the former employee's office manager, Mr. Yox, cited by respondent (Tr. 8491-93; RPF 775(c)(1)), does not refute Mr. Crepeau's testimony quoted in the text that he was induced to exaggerate information. Mr. Yox disagreed with Mr. Crepeau's testimony that the former field representative had once rewritten a report after an earlier version had been returned to him with instructions that it be worded more strongly. (Tr. 1783, 8491-92) Mr. Crepeau, however, did not testify that the practice mentioned in the text was induced by these purported instructions.

Nor is there a direct conflict between Mr. Crepeau's testimony that instructions he received from his manager to "pick up on [his] declines * * * and protectives" affected how he wrote his reports (Tr. 1762) and the testimony of his manager that he did not "expect" Mr. Crepeau to produce a "specified percentage" of declinable and protective information. (Tr. 8490) The former manager testified that he informed his field representatives of the results of the quality audits (Tr. 8490) and Mr. Crepeau may well have inferred from these communications that he was expected to produce more adverse information, whether or not his manager intended to communicate such an expectation.

As noted by respondent, numerous current and former employees testified that the system did not affect the way in which they prepared and wrote their reports. Indeed, some of complaint counsel's witnesses so testified. However, we do not find fault with respondent's procedure because it caused widespread distortion of adverse information. Our conclusion that it did not meet the test set by Section 607(b) is based on the incentives it created for those employees who were either unable or unwilling to make the effort necessary to reach the objective without exaggerating or distorting the information uncovered by their investigations.

Bristol-Myers Co., 85 F.T.C. 688, 743 n.9, 745 (1975); *Coca-Cola Co.*, 83 F.T.C. 746, 809 (1973). However, in view of the difficulties of locating reports containing inaccurate adverse information, regardless of whether such reports exist, and of proving the causes of the inaccurate reporting, we do not believe that the record need contain actual inaccurate reports to sustain a ruling that respondent's procedures were not reasonably designed to assure maximum possible accuracy and conclude that the procedure was inconsistent with Section 607(b).

Indeed, as we have already observed, Section 607(b), rather than prohibiting inaccurate reporting, imposes upon reporting agencies an affirmative obligation to follow "reasonable procedures to assure maximum possible accuracy." It is the failure to follow reasonable procedures, and not the production of inaccurate reports, which violates Section 607(b). We are aware of nothing in the legislative history or the text of the statute which supports respondent's assertion that a reporting agency may not be liable under Section 607(b) unless a challenged procedure is shown already to have resulted in some inaccurate reporting.[22]

Respondent correctly observes, however, that several courts have declined to consider claims that reporting agency procedures failed to meet the standard established by Section 607(b) absent a showing that an inaccurate report had been produced. Our analysis of this issue, however, is not greatly assisted by [16]decisions rendered in private FCRA lawsuits brought by consumers seeking damages for noncompliance with the statute. In private damage actions, it is not surprising that courts will be unwilling to resolve difficult liability issues absent evidence that the alleged violations have resulted in harm to the plaintiff.

The Commission's enforcement role is different from that of the individual consumer seeking to vindicate his or her own rights under the statute. The Commission is directed to treat a violation of any requirement or prohibition imposed by the FCRA as a violation of Section 5 of the FTC Act. It is settled that specific injury need not be shown to establish that a practice is "unfair or deceptive" under Section 5, *see, e.g., Resort Car Rental System, Inc.* v. *FTC*, 518 F.2d 962, 964 (9th Cir.), *cert. denied sub nom. MacKenzie* v. *United States*, 423 U.S. 827 (1975), and Congress has not expressed any intention

[22] Under respondent's construction of the statute, liability could not be established even if on its face, a procedure would mandate the production of inaccurate adverse reports. For example, respondent would seemingly argue that a quota system explicitly requiring each investigator to produce 10 adverse reports each day and, if necessary to meet the quota, to falsify adverse information, could not be challenged unless and until it could be shown that the procedure had actually resulted in the production of inaccurate adverse reports. Such a quota system, however, clearly would not be a "reasonable procedure to assure maximum possible accuracy," and on that basis alone would be a violation of the statute whether or not harm could be shown.

that the Commission be required to establish that an alleged violation of the FCRA has already injured consumers, even assuming Sections 616 and 617 require such proof in cases brought by consumers.[23]

A procedure which encourages the production of adverse information is likely to lead employees to prepare their reports in a manner detrimental to the legitimate interests of the consumers about whom reports are written. This risk was realized in this case. Because we can hardly conclude that procedures which pressure employees to produce adverse information are necessary to the proper operation of consumer reporting agencies,[24] and are unaware of any justification for their use which would outweigh the risks which they pose, we find that they violate Section 607(b).[25]

Although our analysis requires us to conclude that the ALJ was correct in holding that respondent's quality audit procedure violated Section 607(b), it also compels us to find that he erred in holding that the procedure was flawed only because [17]the audits were based on unrepresentative audit data and invalid comparisons among offices.[26] This error resulted in the entry of an order which fails to prevent the abuses which can be expected to result from any procedure placing a premium on the production of adverse information.

The judge reasoned that the methodological flaws had the effect of pressuring some employees, and the potential to pressure many others, to meet goals which, taking account of the special characteristics of the areas they worked, could not be met without their engaging in the practices we have described above. Nevertheless, while the flaws identified by the ALJ increased the likelihood that the system would result in inaccurate reporting, we believe that other systems which promote production of adverse information are likely also to be unreasonable.

Respondent has recognized that its employees vary in their abilities and their diligence. Its President and Chief Executive Officer, denying that the company has set specific quotas for protective or declinable information which should be developed "by a specific man or by a specific territory," testified that "[i]t has been a

[23] We should add that while Section 5 cases can be useful in construing the FCRA, we rely on our understanding of Section 607(b) in concluding that inaccuracy need not be shown. We need not rely on our authority under Section 5 "to arrest trade restraints in their incipiency." *FTC* v. *Brown Shoe Co., Inc.*, 384 U.S. 316, 322 (1966).

[24] That such procedures are dispensable is supported by respondent's decision to discontinue auditing protective and declinable information. *See* p. 8 *supra.*

[25] This violation of the FCRA, and each of the other violations which we find in this case, is also an unfair or deceptive act or practice in violation of Section 5 of the FTC Act. FCRA, Section 621(a).

[26] *See* p. 9 *supra.*

widely accepted thesis that it [the amount of protective and declinable information] varied widely by line of service, by * * * man, by geography, by the type of the environment in which the reports were made and a lot of other factors." He also testified that

> there has never been any feeling that there was that degree of uniformity on pertinent information by line of services, by territory and by individual.
>
> So it would be unfair and inequitable to have a policy that would seek to develop some kind of a quota system or some kind of an average percentage of pertinent information * * *.

Tr. 5017–18, 5068.[27] [18]

Thus, as respondent recognizes, even if most employees can meet a given objective, that is, produce enough adverse information to qualify for a "reward" or avoid a "punishment," by using careful investigative techniques and accurately reporting the information they obtain, the less able, or less diligent, employee may not. These employees, like several of respondent's former employees, when pressed to produce an amount of adverse information which is suitable for other employees, may reasonably be expected to fabricate, exaggerate, or otherwise misreport.

We, therefore, agree with complaint counsel that the order should prohibit any procedure

> whereby the performance of branch offices, regions, or other organizational units, with respect to the production of adverse * * * information is ranked against other organizational * * * units or individuals, or against previous performance by the same organizational units or individuals.

Proposed Order, ¶ II(7) (CAB 80). With some minor alterations, we will adopt this order provision.

We recognize, however, that it is not the surveys themselves which are unlawful, only the pressures their dissemination may be expected to create. Because we believe that rankings and other comparisons of performance are likely to create the kinds of pressures to produce adverse information which are demonstrated by this record, we believe their use should be prohibited, and so order. If respondent can develop a system of sampling which it believes will prevent the kinds of pressures shown on this record, it may, of course, move to modify the order.

Finally, we note respondent's objection to complaint counsel's

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[27] The manager of one of respondent's branch offices, called by respondent, similarly testified that the percentages of protective and declinable information which field representatives will develop vary by the area they work (Tr. 8603; ID 333), and respondent has acknowledged that "field representatives have varying levels of experience and training * * *, [and] work in a variety of geographic areas * * * which have differing characteristics affecting the ease with which reports may be completed * * *." (R. Ans. 48)

proposal that we prohibit it from "compelling or *inducing* its * * * personnel to complete or prepare a *certain* proportion * * * " [emphasis added] on the ground that the words "inducing" and "certain" are vague. (R. Ans. 58–59) We will instead prohibit respondent from rewarding or punishing, or representing that it will reward or punish, employees on the basis of the amount of adverse information they produce, or taking any action to encourage employees to produce any specified number, or proportion, of reports containing adverse information.[28] [19]

2. Production Quotas

The complaint also challenged respondent's imposition of a production quota which requires the field representative to complete a specified number of cases each month. Unlike pressures to produce adverse information, the production quota is not inherently inconsistent with the obligation imposed by Section 607(b).

The parties do not challenge the ALJ's description of the production quotas. Each full-time, salaried field representative is expected to meet a "production standard." The standard is set on a monthly basis and requires the field representative to produce reports which generate revenue exceeding his or her salary and expenses. The amount by which revenue must exceed salary and expenses is a product of the "reporting standard," which varies among the offices and according to the length of service of the particular field representative. Field representatives' monthly production standards are determined by dividing their salary and expenses by their reporting standard; the higher the reporting standard the less revenue the representative is expected to generate that month. (ID 109–11) Much of the evidence adduced at trial was directed to the question whether the company's reporting standards resulted in quotas requiring field representatives to produce so many reports that they were compelled to take shortcuts which sacrificed the accuracy of their reports.[29] [20]

[28] Thus, our order will not preclude respondent from distributing to field representatives information and statistics showing, for example, "the number of alcoholics in the population," (R. Ans. 59) so long as it takes reasonable steps to assure that the field representatives to whom these materials are sent are clearly informed that the materials are for information only and that they are not expected to produce any particular amount of adverse information.

Moreover, the order's prohibition against rankings of performance in producing adverse information (Order, ¶ I.D.) and against rewarding and punishing employees on the basis of the amount of adverse information they produce (Order, ¶ I.C.(1)) will not preclude respondent from *measuring* an individual field representative's production of adverse information and taking the employee's low production as a signal that the employee may be failing to investigate his or her cases carefully. Paragraph I.C. (1), however, would require that respondent base any adverse action against an employee on a determination that the employee is defaulting on his or her obligation to produce accurate rather than adverse reports.

[29] Management expects field representatives to meet their production standard on a quarterly basis, unless the failure can be justified by factors beyond the employee's control. (ID 114) Management also expects field

(Continued)

Although field representatives receive their normal compensation even if they fail to meet their production standard, the ALJ found that field representatives are aware of the existence of the standards, that managers of the branch offices have occasionally acted to enforce the standards, and that the standards have affected the manner in which some employees have done their jobs.[30]

The ALJ held that use of the quotas violated Section 607(b) because "[a] substantial number of field representatives * * * were unable to complete the work in either the normal workday or workweek in accordance with Company procedures. They compensated for such inability by contacting unqualified sources, faking sources, misstating time coverage, hurrying through interviews, failing to ask a full range of questions, using the telephone in a manner not in accord with Company procedures, or working excessive overtime * * *." (ID 405)

Although the ALJ found that "[g]enerally field representatives did not fake sources in those instances where unfavorable * * * information was developed" (ID 402) and that "there is no evidence in the record of a report where *adverse* information has been falsified" (ID p. 243) (emphasis added), he concluded that the procedure was unreasonable; according to the judge, Section 607(b) does not distinguish between adverse and favorable reports. (*Id.*)

Respondent first challenges the ALJ's finding that a substantial number of employees have been unable to meet their [21]production requirements without resorting to shortcutting techniques. Judge von Brand relied principally on the testimony of 16 former employees called by complaint counsel. He found unpersuasive respondent's proof, including several statistical studies and the testimony of a number of present and former employees that they were able to meet their production quotas.

We affirm the ALJ's findings as to the credibility of complaint counsel's witnesses.[31] We also find that the testimony offered by these witnesses demonstrates that a substantial number of employees could not meet their quotas without "cutting corners." Testimo-

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representatives to prepare their reports in accordance with "Time Service" objectives which require that an office, within a set time after receiving a request for a report, complete it and mail it back to the requesting customer. Branch managers have been told that "[t]ime is an essential and marketable element of our business" and records have been maintained to measure an office's performance. (ID 348, 352)

Although part-time field representatives are compensated on the basis of the number of reports they actually produce (ID 130) and, accordingly, are not expected to produce a certain number of reports to justify their salaries, a part-time employee might "cut corners" in order to produce enough reports to meet Time Service objectives. (ID 384)

[30] One branch office manager testified that he might give a field representative who falls behind the production standard "a boost or a kick and possibly assign him an extra case per day or whatever it will take, whatever is necessary to bring him into the black." (ID 347)

[31] *See* note 17 *supra.*

ny by other witnesses that *they* could meet *their* quotas does not undercut this limited finding; nor is it rebutted by the statistical evidence offered by respondent showing, at most, that the *typical* field representative could work enough cases to meet his or her quota.

Respondent also challenges the ALJ's holding that a procedure which does not promote the production of inaccurate reports containing *adverse* information about consumers nevertheless can properly be found to violate Section 607(b). We find respondent's argument persuasive. The expressions of congressional purpose behind the FCRA clearly demonstrate that the statute was intended to curtail the reporting of inaccurate *adverse* information.[32]

The ALJ found little evidence that the production quotas increased the production of reports containing inaccurate adverse information. We agree that evidence of such an effect is scant, [22] but for the reasons stated earlier, *see* pp. 14–15 *supra,* do not consider the amount of evidence of actual harm dispositive. Rather, we must examine the incentives which respondent's practice is likely to create. Here, there is evidence, presented by complaint counsel's own witnesses, showing that, while field representatives often took shortcuts in reporting *favorable* information (for example, by misreporting the number of sources whom they had contacted),[33] they were careful not to fake adverse information. (*E.g.,* Tr. 316, 1837) We suspect the reason is that field representatives knew they were more likely to get caught faking unfavorable information.

The FCRA permits the consumer to learn the "nature and substance" of the information in his or her file and requires reporting agencies to reinvestigate information disputed by the consumer. It is apparent that field representatives, absent overriding pressures, such as those created by the audits, are deterred from

[32] *See* pp. 6–7 *supra.* The concern about preventing harm to the subjects of reports is also reflected in the statement of purpose which accompanied the statute:

> It is the purpose of this title to require that consumer reporting agencies adopt reasonable procedures for meeting the needs of commerce for consumer credit, personnel, insurance, and other information *in a manner which is fair and equitable to the consumer* * * *.

FCRA, Section 602(b) (emphasis added).

Section 602(a)(1), recognizing the banking system's dependence upon accurate credit information, should be read in conjunction with Section 602(b) and the legislative history; it, therefore, does not persuade us that this consumer protection measure was designed to proscribe procedures which are not likely to harm the consumer about whom a report is written.

[33] We do not mean to suggest that this is necessarily a good result. The individual about whom an overly favorable report is written may or may not benefit, but the businesses which depend on accurate information may be harmed, and consumers as a group may be required to subsidize the bad risks who are extended credit or insurance. However, there is little reason to doubt that the customers of reporting agencies can protect themselves against the harm resulting from excessive under-reporting of adverse information.

falsifying adverse information, because reports containing such information are more likely to be challenged and reinvestigated.[34] The supposed failure of evidence with respect to the pressures to produce adverse information, *see* p. 14 *supra,* was not inconsistent with a finding of a violation of Section 607(b); nevertheless, our understanding of the reason for the lack of evidence of harm flowing from the production quotas—and the corroborative testimony offered by complaint [23]counsel's own witnesses—requires us to conclude that the production quotas do not violate Section 607(b).

We recognize, however, that there are some risks inherent in the combined imposition of production quotas and pressures to produce adverse information. The combination of production quotas and pressures to produce adverse information has the potential to encourage the preparation of a larger number of reports containing adverse information than would be completed absent these combined procedures.[35] The development and confirmation of adverse information is generally more time-consuming than the development of favorable information (ID 375), at least when care is taken to ensure that the information is accurate. Accordingly, there is a substantial risk that employees, pressed simultaneously to do more work and to prepare more reports containing adverse information, will be induced to save time by reporting adverse information which they have either faked, exaggerated, or failed to confirm.

We are sensitive, however, to the fundamental needs of firms to promote productivity and we do not lightly curtail such efforts. Since production quotas, at most, may exacerbate the evil inherent in the imposition of pressures to produce adverse information, this risk will obviously be dissipated by our prohibition of the imposition of such pressures. We are not persuaded of the need for additional relief.

3. Production Credit and Compensation for Reinvestigations

Complaint counsel appeal from the ALJ's dismissal of the com-

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[34] It is respondent's policy to fire employees who are found to fabricate report information. (ID 407) Although the ALJ found that the production quotas have induced employees to take shortcuts other than fabricating sources and other report information, such as "hurrying through interviews" and "using the telephone in a manner not in accord with Company procedures," (ID 405; p. 20, *supra*) there has been no showing that these shortcuts would likely induce the misreporting of adverse information. (As to the use of the telephone, *see* pp. 80–81 & n.107–08.)

It does not appear that the kind of distortion or exaggeration likely to be induced by the pressures to produce adverse information, discussed at pp. 12–14 *supra,* is generally a firing offense.

[35] The production quotas require employees to produce more reports than they might otherwise. The adverse information pressures induced employees to see to it that specified percentages of all of the reports they prepared included protective or declinable information.

plaint's challenge to respondent's alleged policy of paying or crediting[36] a field representative for a reinvestigation conducted pursuant to Section 611 of the FCRA[37] only if the reinvestigation [24] proves that the employee was correct in the initial investigation. Complaint counsel contend that the policy provided field representatives an incentive to try to prove they were right the first time and, therefore, discouraged the correction of errors in the original report. We affirm the ALJ's dismissal of this claim. Field representatives handle only a few reinvestigations each month and there has been no showing that the loss of the few production credits or the small amount of compensation involved would provide employees a meaningful incentive to conduct inadequate reinvestigations or to misreport the results.[38]

Indeed, a field representative could be expected to fear that any misreporting of the results of a reinvestigation would be detected by the consumer whose dispute of the original information triggered the reinvestigation. Although the prospects of detection are uncertain, we doubt that the modest incentive to falsify information afforded to the investigator by the challenged procedure would offset the risk of his or her being caught by a consumer who has already complained about the information in question and who might be expected to be skeptical about the results of the reinvestigation.[39] Therefore, we find that the procedure [25]is consistent with Section 607(b).[40]

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[36] Only part-time field representatives are paid on the basis of the number of reports they prepare. Full-time field representatives are salaried but are expected to meet the production standard described at p. 19 *supra*. At issue here is respondent's alleged failure to compensate the part-time field representatives and to give the full-time employees production credits for their reinvestigations when the original report is found to be inaccurate.

[37] The reinvestigation requirement is described at pp. 42–47 *infra*.

[38] If the compensation system could be expected to affect the manner in which field representatives conducted their reinvestigations and worded the results, it could also be expected to provide them an incentive to do an accurate job in the first place.

Although complaint counsel offered a few examples of misreporting which may have occurred as a result of the procedure, this scanty evidence does not convince us that the procedure is unreasonable. Although a few *law violations* are sufficient to warrant issuance of an order, *see* p. 33 *infra*, here, the alleged law violation is the use of an unreasonable procedure. That a procedure may induce a handful of employees to produce inaccurate reports does not establish that the procedure itself is unreasonable. Proof of some inaccurate reporting is neither essential nor necessarily sufficient to sustain a finding of a violation of Section 607(b). *See* p. 15 *supra*.

For this reason, although we affirm the final sentence of finding 507 that "[t]here is insufficient detail * * * in this record to determine that a pattern of inaccurate reporting has taken place by virtue of such compensation procedures," we do not believe that this lack of evidence would, by itself, preclude a finding of violation.

[39] The ALJ found that the impact of the failure to provide production credit or compensation may be especially great "in those areas involving subjective judgment on the part of the field representative * * * where differences of opinion are possible, [and] there would be a tendency to deny the consumer the benefit of the doubt * * *." (ID 507) He correctly found, however, that in such cases, it is respondent's policy generally not to assign a reinvestigation to the field representative who conducted the original investigation. (ID 496) In any case, the impact of the practice of denying credit or compensation has not been shown sufficient to affect the conduct of the reinvestigation.

[40] The ALJ understood that the case had been presented to him on the theory that the interaction of various company procedures and policies, such as the production quotas, time pressures on field representatives, the methods by which employees are compensated, and the inducements to produce adverse information, could result in the misreporting of consumer report information. (ID p.233) On appeal, however, complaint counsel have elected essentially to challenge separately the reasonableness of the various procedures and have not attempted to show

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4. Health and Arrest Information

Complaint counsel attempted to prove at trial that the collection of health and arrest information from lay sources, that is, neighbors and other acquaintances who do not have formal training or professional experience in assessing people's health or the nature of their contacts with the criminal justice system, is inconsistent with respondent's obligation to follow reasonable [26]procedures to assure maximum possible accuracy. The ALJ found that the record does not support complaint counsel's claim.

Reliance on lay sources for such technical and sensitive information is highly troublesome.[41] Indeed, the Privacy Protection Study Commission has observed that "[c]ollection of such technical information [*i.e.,* health information that only a professional is competent to report] from anyone other than the individual himself, a medical source, or a close family member invites inaccuracies." U.S. Privacy Protection Study Commission, *Personal Privacy in an Information Society* 178 (1977). The reporting of arrest information and other information about an individual's criminal record raises the same concerns.

Nevertheless, with the limited attention that was directed to this issue at trial and in the briefs filed with the ALJ and the Commission, we cannot conclude that the manner in which respondent has relied upon lay sources is incompatible with Section 607(b).[42] Indeed, basic common sense would suggest that, in certain instances, neighbors and other acquaintances are capable of being reliable sources for information about a person's health or criminal record. Their reliability might depend on a variety of factors, including the kinds of information they are reporting, *their* sources (first-hand observation, the applicant, members of the applicant's family, as opposed to mere gossip) and any biases which may affect

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how the procedures, in combination, risk the misreporting of information. (Of course, time pressures and the method by which field representatives are compensated are part and parcel of their challenge to respondent's production quotas.)

We have not ignored the possible interaction of these policies and procedures, *e.g.,* p. 23 *supra,* but conclude that, whether viewed separately or in juxtaposition with the other challenged procedures, the production quotas and the method of compensating employees for reinvestigations have not been shown to violate Section 607(b).

[41] A person may display symptoms entirely unrelated to the illness or injury to which a lay witness may ascribe them— for example, a person may appear drunk when suffering from a diabetic reaction. Similarly, the occurrence of an arrest may inaccurately be inferred from actions which in themselves lack any legal significance, such as the person's entering a police cruiser in the company of law enforcement personnel or a police officer's presence at the person's house for reasons unrelated to criminal law enforcement.

[42] Respondent appears to acknowledge that official records are the most reliable source of information on an individual's criminal record. (R. Ans. 24) Failure to confirm such information through official records in those cases where they are available could not be part of a reasonable procedure to assure maximum possible accuracy. Complaint counsel have not satisfied their burden of proof that respondent has failed to instruct field representatives to confirm this information through official records, where available, or that the representatives have not complied with the company's instructions.

the credibility of either the informant or [27]the informant's sources.[43] Here, we do not have a record which permits us to define, with any precision, the circumstances in which lay sources may not properly be used, to determine whether respondent has in fact depended upon lay sources in those circumstances, and even if we could find that it had, to fashion a meaningful remedy.

Despite our concerns about the use of lay sources, we cannot find a violation on the basis of this record and therefore affirm the ALJ's findings.

B. Refusals To Disclose Files to Consumers and To Reinvestigate Disputed Information

The complaint contains a number of allegations concerning the respondent's duty to disclose information to consumers and its concomitant responsibility to reinvestigate disputed information and correct inaccuracies. In enacting the FCRA, Congress recognized that, no matter how careful consumer reporting agencies are to avoid error, some inaccuracy is inevitable. As Senator [28]Proxmire noted when the consumer credit bill was introduced in the Senate:

> It would be unrealistic to expect credit reporting agencies to be absolutely correct on every single case. But it seems to me that consumers affected by an adverse rating do have a right to present their side of the story and to have inaccurate information expunged from their file. Considering the growing importance of credit in our economy, the right to fair credit reporting is becoming more and more essential. We certainly would not tolerate a Government agency depriving a citizen of his livelihood or freedom on the basis of unsubstantiated gossip without an opportunity to present his case. And yet this is entirely possible on the part of a credit reporting agency. 115 *Cong. Rec.* 2412 (1969).

Therefore, besides mandating the use of "reasonable procedures to assure maximum possible accuracy of the information concerning the individual about whom a report relates," Congress imposed a variety of procedural requirements intended to enable consumers to

[43] A reasonable procedure to assure the maximum possible accuracy of this information would, at the very least, attempt to ensure that field representatives do not rely on lay sources when, because of the sources' own particular limitations, or the nature of the information being reported, the sources are unlikely to be reliable. Field representatives should not be expected to make these judgments on an *ad hoc* basis; a consumer reporting agency which was interested in preventing the misreporting of such sensitive information would at least provide its employees with instructions which would guide them in making these difficult judgments.

This case was not tried on the theory that respondent failed to meet this obligation, but we wish to emphasize that we take no comfort from the instruction quoted by the ALJ, at ID 517, which provides in part:

> when reporting * * * [arrest] information [and local police records are unavailable], put it in the same language as we developed it, such as "there is talk in the community that your subject has had police difficulties, but police records are not available to verify this information."

Such an instruction can hardly suffice to alert field representatives to the factors they should consider in assessing the reliability of a source's account of such vague, and potentially damaging, information.

identify and correct inaccurate information. We agree with the comment that a major goal of the FCRA "is the creation of a system of 'due process' under which consumer subjects may learn of adverse reports, be confronted with the information therein, and be able to correct or supplement false or misleading entries." Note, *Judicial Construction of the Fair Credit Reporting Act: Scope and Civil Liability,* 76 *Colum. L. Rev.* 458, 466 (1976).

Compliance with the consumer disclosure, reinvestigation and correction provisions of the statute is fundamental to achievement of Congress' goal of assuring "maximum possible accuracy" in consumer reports. For the scheme to work, however, consumers must have ready access to the information, for disclosure is the trigger for the other corrective provisions. Additionally, in enacting the FCRA, Congress intended not only to prevent consumer reporting agencies from flatly refusing to disclose information to consumers, but also to bar the use of more subtle techniques to achieve the same end.[44] [29]

While the record shows that respondent has, commendably, gone beyond the requirements of the Act in some respects,[45] it also shows that respondent's employees have engaged in violations of the statute which warrant an order to cease and desist.

1. Failure To Disclose "Nature and Substance" of Information in Respondent's Files

Section 609 of the FCRA requires consumer reporting agencies, upon request and proper identification, to disclose to the consumer the "nature and substance" of all information (except medical information) in its files on the consumer at the time of the request, the sources of the information,[46] and the recipients of any report on the consumer which the reporting agency has furnished for employment purposes within the two-year period preceding the request, and for any other purpose, within the six-month period preceding the request. The complaint alleged that respondent has violated Section

[44] The Senate report illustrates these concerns:

> Credit bureaus sometimes build roadblocks in the path of the consumer. For example, the credit bureau industry trade publication, in frankly discussing this problem, states that some bureaus discourage consumer interviews "by placing a nuisance charge on the investigation, or merely placing the date of the interview as much as 2 weeks away."

S. Rep. No. 91-517, *supra*, at 3.

[45] The record shows, for example, that since June 1974, it has been respondent's policy to provide consumers who visit its branch offices visual disclosure of their files. (RX 576 A-E) Since October 1976, it has also been respondent's policy to supply copies of reports to consumers after they have had visual access or, in the case of telephone disclosure, on a subsequent visit to the office. (Copies are normally furnished, however, only if the consumer agrees with the report.) (RX 122A, C-E) In addition, the record shows that respondent sometimes waives the payment by the consumer of the disclosure fee authorized by the statute. (ID 560)

[46] A consumer reporting agency may refuse to disclose investigative sources.

609 by failing to make full and accurate disclosures to consumers upon request.

The ALJ found that respondent's practice varies among offices. While employees in some offices have gone beyond the statutory requirements and provided *verbatim* disclosures, in others, they have disclosed "a summary or paraphrase of the report" or "only the part of the report which the discloser 'assumed was the factor' that [30] had caused the consumer to be rated or denied insurance * * *." (ID 541)[47]

Moreover, "[i]n practice, some field personnel, while purporting to give the nature and substance of reports, failed to give adequate or complete disclosure." (ID 542) Important omissions from the disclosures included references to various consumers' being "said to be a fast and careless driver," having a drinking problem, and having "questioned" morals. (ID 543, 547)

The judge also found that some employees paraphrased or summarized items "in such a way that the full meaning, and in some cases, the derogatory tone of the report, was not conveyed to the consumer." (ID 551) For example, one consumer was told that, according to her report, she "had recently had a run-in with [her] former husband, a severe one," while the report actually stated that she had been assaulted by her husband and incurred 22 stab wounds as a result. (ID 553)

Respondent argues that, in many of the instances of incomplete disclosures relied on by the ALJ, the evidence is insufficient to support the finding of a violation. (RAB 80) We believe, however, that the omissions and dilutions of derogatory information found in this record are violations which go to the heart of the Act's procedural scheme.[48] Such practices are totally [31]inconsistent with

[47] We are not persuaded, as claimed by complaint counsel, that respondent's management instructed its office personnel to tone down or omit from disclosure derogatory information contained in the reports.

[48] **Respondent challenges several of the findings of incomplete disclosure. We affirm each of the challenged findings, except for ID 544, 552 n.208, and ID 550. The witnesses cited in the first two findings testified that they had** inquired why their policies had been canceled or denied. Respondent was under no duty to disclose information which, for all we can tell from the record, did not contribute to the insurer's decision. As noted at p. 32 *infra*, a consumer who requests disclosure of his or her file or of a report is entitled to more than a reading or a paraphrasing of the portions which respondent's staff believes relevant to the particular adverse action which prompted the consumer's inquiry, and the reporting agency may not assume that a consumer who requests disclosure of his or her file is only interested in why a particular adverse action was taken. There is no reason, however, to require disclosure of the entire file when the consumer plainly expresses an interest in only a portion of it. ID 550 was apparently based on a mistaken belief that the consumer's testimony was unrebutted. (ID 550 n.207) Because it was contradicted by one of respondent's witnesses (Tr. 8336-37) and the ALJ has made no assessment of the relative credibility of the two witnesses, we will vacate this finding.

We are persuaded that ID 546 n.203 properly addresses the objections respondent raises to Mr. Smith's testimony.

The subsequent deletion of the information described in ID 552 is not inconsistent with the ALJ's finding that it was not disclosed. The consumer's challenge to the general information which was disclosed placed respondent on notice that she also disputed the more specific information which was not disclosed. That the general disclosure prompted this consumer to challenge its accuracy does not mean that the disclosure was adequate. Section 609 does

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Section 609's mandate that, at the consumer's request, the reporting agency disclose the "nature and substance of *all* information * * * in its files at the time of the request." (emphasis added)

Section 609 should be interpreted, according to the House conferees, "to permit the consumer to examine all the information in his file except for sources of investigative information, while not giving the consumer the right to physically handle his file." H.R. Rep. No. 91–1587, 91st Cong., 2d Sess. 29 (1970).

When information is not disclosed, the consumer obviously cannot determine whether the information should be disputed. Similarly, when the discloser tones down adverse information in the file, the consumer is deprived of the opportunity to challenge the manner in which the agency has chosen to report it. If the FCRA's objective of curtailing the reporting of inaccurate information is to be achieved, consumers must be afforded an uncensored view of the information in their files.

Although we cannot conclude that the FCRA requires a reporting agency to allow consumers to inspect their files or to make *verbatim* disclosures of file information, if Congress' objective is to be achieved, the disclosures must be sufficiently detailed to enable consumers to question the accuracy of the information if they believe it is inaccurate. The omissions and dilutions shown in this record resulted in clear-cut failures to meet this standard. We recognize that the task of determining how detailed the disclosures must be may not be an easy one for a reporting agency's employees. Thus, while we will not require such a procedure, it may well be that the

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not permit a reporting agency to guess whether a generalized disclosure will afford a consumer notice that the report may contain inaccurate or incomplete information. Similarly, ID 554 is not shaken by the fact that a reinvestigation was undertaken. In addition, the ALJ's finding is supported by the testimony of respondent's witness, who made the disclosures in question. As to ID 547 n.204, holding that respondent was under a duty to show that an undisclosed report was not in its files, we observe that complaint counsel established that, at the time the witness requested disclosure, a report was in existence. Since reports would customarily be found in respondent's files, *see* RPF 46, 46(b), the burden shifted to respondent to show that this consumer's report was not, in fact, somewhere in its files. It is immaterial whether the report was in the file of the particular office to which the witness directed her request for disclosure, since Section 609 plainly requires that, upon request, *the consumer reporting agency* must disclose the nature and substance of all information (except medical information) in *its* files. The term "file" "when used in connection with information on any consumer, means all of the information on that consumer recorded and retained by a consumer reporting agency regardless of how the information is stored." FCRA, Section 603(g).

We note that the parties disagreed at trial whether the report at issue in ID 549 was a "business report." (Tr. 3714–18) Respondent, however, has not challenged the ALJ's finding on appeal on the ground that the information was not disclosable as a business report.

We also reject respondent's assertions that several of the findings should be set aside because the information omitted from the disclosure was insignificant. *See* discussion *infra*. Nor is the possible inadvertence of the omissions material. In contrast to Sections 606 and 615, Section 609 does not provide for a defense of good faith. *Cf. Certified Building Products, Inc.*, 83 F.T.C. 1004, 1041–42 (1973), *aff'd sub nom. Thiret* v. *FTC*, , 512 F.2d 176 (10th Cir. 1975).

Finally, we reject respondent's challenges to several findings (*e.g.*, ID 545–46, 548) insofar as respondent asserts that the ALJ erred in giving credence to a consumer witness' recollection. *See* note 17 *supra*.

most prudent way for respondent to ensure compliance with the Act will be to provide *verbatim* disclosure over the telephone[49] just as it [33]now allows consumers who visit its branch offices to observe the contents of their files.[50]

Respondent argues that, assuming all of the ALJ's findings of individual violations are correct, they do not show that respondent has been guilty of such widespread violations that the entry of an order is justified. According to respondent, "[t]hese findings are based on only 13 alleged violations in 11 of respondent's more than two hundred branch offices." (RAB 79) The magnitude or frequency of prohibited activity, however, is not germane to whether the activity is, in fact, illegal, although it may be relevant to the nature of the relief. As we said in *Peacock Buick, Inc.*, 86 F.T.C. 1532, 1554 n.4 (1975), *aff'd*, 553 F. 2d 97 (4th Cir. 1977), "The facts that it was not respondents' general policy to misrepresent, and that in many cases there may have been no misrepresentations, do not in themselves negate direct testimony that in particular cases misrepresentation did occur." The same principle necessarily extends to other types of violations. We, therefore, will not excuse the incomplete disclosures shown in this record simply because, in other instances, perhaps even a majority of other instances, adequate disclosures may have been made.

We also uphold the ALJ's determination that respondent has discouraged disclosures by imposing conditions on disclosure, principally requesting the consumer to sign a form (CX 337) authorizing respondent to investigate any matter the consumer might dispute and authorizing "any business, organization, professional person or anyone else to give full information and records about" the consumer.[51] Although the ALJ found that when consumers refused to sign the form, they were given disclosure anyway, an examination of the form satisfies us that consumers would have understood that they were required to sign in order to obtain disclosure. Since the statute does not authorize the conditioning of disclosure upon the signing of such an authorization, obliging consumers to execute this form, or inducing them to believe they were required to sign, amounted to a violation of the FCRA.[52] [34]

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[49] Several of respondent's witnesses testified that this is, in fact, their practice. (*E.g.*, Tr. 11081, 11671)

[50] In those instances where a reporting agency uses codes or other terminology in its reports which may otherwise be unintelligible to the consumer, disclosure of the "nature and substance" of information may require its employees to explain the information to the consumer; *verbatim* disclosures may not suffice. *See* FCRA, Section 610(c).

[51] The practice was discontinued in 1974 or 1975. (ID 535 n.194)

[52] Respondent argues that "[e]ven if signing the form was a condition, the Administrative Law Judge failed to explain why the consumer seeking disclosure has a legitimate right to withhold the permission to reinvestigate disputed information." (RAB 85 n.82) Although the reporting agency is under a duty to reinvestigate information which the consumer disputes, a consumer might well have legitimate reason to refuse to allow respondent access to

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Finally, we affirm for the most part the ALJ's findings that in some instances respondent's personnel have engaged in outright refusals to make disclosure.[53] These findings, together with the [35] findings that respondent has imposed improper conditions upon disclosure and made incomplete disclosures, warrant the order provisions prohibiting respondent from failing to provide the "nature and substance" of the information in consumers' files so long as they meet the conditions set forth in Sections 609 and 610. We are not, however, persuaded by complaint counsel that we should require respondent to provide consumers with actual copies of their reports upon request.[54]

2. Failure To Make Disclosure of Claim Reports

A second element of respondent's alleged failure to comply with the FCRA's disclosure requirements involves non-disclosure of reports used by insurance companies to assess the validity of claims under policies, or "claim reports."[55] Complaint counsel argue that respondent's claim reports are disclosable for two reasons. The first is that respondent, at least for a time (ID 588, 594; RPF 977-78, 980, 986), filed its claim reports with its other reports, including consumer reports, in a single reference filing system and permitted

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any and all information (including medical information) the agency might deem relevant to a reinvestigation.

The record also supports the ALJ's finding (ID 537) that respondent refused one witness' request for disclosure unless he first obtained a "written authorization" from his insurance company. (Tr. 3110-11) Respondent has not offered any support for its assertion that the consumer was refused disclosure simply because he refused to pay the charge permitted by Section 612 and to give written permission for disclosure to be made in the presence of a third party pursuant to Section 610(d). (*See* ID 531.)

[53] We affirm findings 529-33, but qualify our affirmance of finding 532 insofar as it implies that respondent was under a duty to disclose to consumer McCune information solely about his wife. We also do not affirm finding 530 to the extent that it holds that respondent was under a duty to disclose to a consumer who had asked why her insurance policy had been canceled information which could not have contributed to the cancellation. Respondent, however, was under a duty to disclose derogatory information in the report concerning the consumer's husband; this information appeared in a report which purported to be about the consumer and the information apparently was used to cancel her policy. (CX 133) This, accordingly, was "information * * * on the consumer" seeking disclosure. FCRA, Section 609(a)(1).

We also uphold the ALJ's finding that respondent's failure to advise the McCunes (or at least Mrs. McCune) that a report was being prepared or an investigation conducted "discouraged disclosure in a manner tantamount to refusal to disclose * * *." (ID 533) As discussed at pp. 40-41 *infra*, conduct which falls short of an outright refusal may have the same effect. Informing a consumer who requests disclosure that no file exists, without disclosing that a file is being prepared or that an investigation is underway, may effectively foreclose disclosure unless the consumer persists in requesting disclosure or somehow later learns that a file has been prepared.

[54] Nor are we persuaded that we should upset the ALJ's conclusion that respondent's failure to disclose the identities of noninvestigative sources of information and recipients of reports, absent a specific request by the consumer, was consistent with Section 609.

[55] We do not understand respondent, at RAB 85-86, to challenge the ALJ's findings that respondent has actually failed to disclose claim reports in response to requests by consumers for disclosure. We note, however, that the ALJ did not hold that "respondent's position that claim reports, business reports, and some property reports are not subject to the disclosure requirements of the FCRA" itself violates the statute (RAB 85), but instead properly inferred from that position and respondent's own statement that "on *some* occasions, in order to accommodate consumers, claim reports have been disclosed," (RPF 810(a)) (emphasis added) that in other instances disclosure has not been made. (ID 559) According to the ALJ, respondent's "stated position and policy * * * demonstrates the violation." (ID p. 258 n.248) The ALJ also found two instances of failures to disclose and respondent has not challenged the validity of that finding. (ID 559 n.211)

access to both by employees whose job it was to compile consumer reports (other than claim reports). The second is that respondent allowed cross-use of claim and underwriting information, so that claim reports could be said to have been collected and used in whole or in part in the preparation of consumer reports. (C. Ans. 58–59) Thus, according to complaint counsel: [36]

> Respondent's procedures result in a layering of information between underwriting reports and other reports to the point where it would be impossible for respondent to determine where a particular item of information was first obtained, in an underwriting report or some other report. Thus, it is clear that all of these reports should be considered consumer reports, and for that reason subject to the Act's disclosure provisions.

C. Ans. 59.

Respondent asserts that the disclosure requirements of Section 609 apply only to "consumer reports" and that "claim reports, business reports, and some property reports" may not properly be considered to be "consumer reports," either under the plain language of the statute or consistent with its legislative history. (RAB 85–88) Respondent acknowledges that Section 609 "should be read as requiring disclosure to the consumer * * * [of] information which can be said to have been collected in whole or in part for use in a consumer report," but it adds that information collected *solely* for business or other non-consumer reports (for example, claim reports), need not be disclosed to a consumer. (RAB 88) Proceeding on this assumption that claim reports are, by their very nature, "non-consumer" reports, respondent then argues that a finding that claim reports *become* consumer reports would be inconsistent with portions of the legislative history which demonstrate that Congress intended that information relating purely to business transactions not be covered by the statute.

The ALJ, as respondent points out, "does not reject respondent's position that certain reports are not consumer reports, but rather bases his finding of a violation on a refusal to disclose, *assuming* they are *not* consumer reports." (RAB 86) (Emphasis in original) Thus, the judge held:

> The language of Section 609 and Section 603 is clear. It does not limit the disclosure section to consumer reports. Had Congress so intended, it could easily have provided for such limitations. Thus, all information, including information in the reports other than consumer reports, in a consumer reporting agency's files (except medical information) is subject to the disclosure provisions.

ID p. 259.

This case was not presented to the ALJ or to the Commission on

the theory that claim reports are, in themselves, consumer reports, regardless of how they are filed or whether they are used in [37] connection with the preparation of other (consumer) reports. *Compare Beresh* v. *Retail Credit Co., Inc.,* 358 F. Supp. 260 (C.D. Cal. 1973) *with Cochran* v. *Metropolitan Life Ins. Co.,* 472 F. Supp. 827, 831 (N.D. Ga. 1979); Note, *supra* p. 28 at 478–80. Complaint counsel argue, rather, that claim reports "become" consumer reports if they are available for use in the preparation of consumer reports.

We do not reach the question whether those claim reports which were available for use in consumer reports—respondent in 1975 initiated a separate filing system which now apparently prevents interchange of information between the two types of reports (ID 594)—should be treated as consumer reports. We find it unnecessary to reach this question because we agree with the ALJ that Section 609 does not limit a reporting agency's disclosure obligation to consumer reports.

Section 609(a) requires disclosure of the "nature and substance of all information (except medical information) in [the reporting agency's] files on the consumer at the time of the request." The statute, in turn, defines "file" "when used in connection with information on any consumer * * * [as] all of the information on that consumer recorded and retained by a consumer reporting agency regardless of how the information is stored." FCRA, Section 603(g). If this language is to be accorded its natural meaning, it must be construed to require more than disclosure of the consumer reports in an individual's files. *See Fernandez* v. *Retail Credit Co.,* 349 F. Supp. 652, 655 (E.D. La. 1972). Because we can discern no reason to exclude from the literal terms of the statute the claim reports which have been the focus of this proceeding, reports prepared in response to claims made by consumers, the provision of our order requiring disclosure of the "nature and substance of all information * * * in [respondent's] files on the consumer" should be understood to require disclosure of these reports.[56]

3. Telephone and Suboffice Disclosure

The complaint alleged two violations of the FCRA provision that sets forth the conditions under which consumers may obtain the disclosures mandated by Section 609. Section 610 of the Act[57] [38]

[56] Despite the broad language at ID pp. 258–59, both the record and the ALJ's findings (ID 521–59) focused on the duty to disclose consumer reports and consumer-related claim reports. Our order should not be construed to require disclosure of other information.

[57] Section 610 of the FCRA provides in pertinent part:

(a) A consumer reporting agency shall make the disclosures required under section 609 during normal business

(Continued)

directs consumer reporting agencies to make the required disclosures "during normal business hours and on reasonable notice." It further provides that consumers may choose to obtain disclosure of information in person at the consumer reporting agency or by telephone. The statute requires the consumer to provide adequate identification in either case, and it requires, further, that the consumer be granted telephone disclosure if such a disclosure is first requested in writing.

The complaint alleged that respondent has violated its responsibilities under Section 610 by refusing to provide or by discouraging consumers from obtaining disclosure over the telephone and by refusing to make disclosures at some of its so-called suboffices. The ALJ sustained the allegation concerning telephone disclosure, but he dismissed the charge involving disclosures at suboffices. Respondent appeals from the violation found by the judge, and complaint counsel appeal from the dismissal of the charge concerning suboffice disclosure. We affirm Judge von Brand's disposition of both issues.

a. *Telephone Disclosure*

Respondent's major challenge on appeal is that the record contains no evidence that respondent refused to provide telephone disclosure when it had first received a written request for it as required by the statute, and that, consequently, the finding of a violation of Section 610 is not justified.[58] [39]

Respondent is correct that the record does not show that the company, after receiving written requests, has flatly refused to grant telephone disclosures.[59] The record does, however, contain numerous instances in which respondent affirmatively discouraged telephone disclosures in a way that effectively precluded consumers from exercising their rights under the Act. (ID 562–66) The ALJ found that "respondent advised consumers obviously interested in learning what was in their files that disclosure was available in a Retail [Credit Company] office without mentioning the possibility of telephone disclosure." (ID 567) Specifically, he found instances

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hours and on reasonable notice.

(b) The disclosures required under section 609 shall be made to the consumer

(1) in person if he appears in person and furnishes proper identification; or

(2) by telephone if he has made a written request, with proper identification, for telephone disclosure and the toll charge, if any, for the telephone call is prepaid by or charged directly to the consumer.

[58] Respondent also appears to argue that even if the record shows some instances where telephone disclosure did not occur under circumstances in which it was required under the FCRA, the fact that the company makes numerous disclosures by telephone excuses any failures to do so shown on the record. (RAB 89–90) As we have made clear elsewhere in this opinion, we do not accept such an argument as valid. *See* p. 33 *supra*.

[59] Complaint counsel do not contend that respondent refused to honor any written requests it may have received.

where consumers who asked how to obtain disclosure were told that "the only way disclosure could be given was in person," (ID 564) that "disclosure could not be given by telephone," (ID 564) and that "they could receive disclosure of their files at the branch offices." (ID 566) In these instances, respondent did not mention that, upon submitting a written request, the consumer could obtain disclosure by telephone. (*Id.*) The judge also found that, in some instances, "[e]ven though telephone disclosure was not specifically requested * * *, respondent, by undertaking to advise consumers of their rights regarding disclosure and only partially advising them as to their rights has, in a practical sense, made telephone disclosure unavailable to them in violation of Section 610 of FCRA." (ID 567)

Respondent argues that this latter legal theory is "novel" and "totally invalid," in that Section 610 does not impose any requirement on the consumer reporting agency to advise consumers on how to obtain disclosure. (RAB 89-90) We, however, agree with Judge von Brand that when respondent stated or implied to consumers that disclosure could only be obtained by coming to the office (ID 563-64, 566), it effectively denied consumers the option of seeking and receiving telephone disclosure. (ID p. 261)

A consumer reporting agency interested in complying with the law should avoid statements or omissions that would clearly have the effects of misleading the consumer and of foreclosing the consumer's exercise of his or her rights. Indeed, reporting agencies should make every reasonable effort to help consumers understand what they must do to obtain disclosure. We do not find, however, that respondent was under a legal duty to provide consumers with advice on how they might obtain disclosure by [40]telephone or that "if any statement is made to explain 'the availability of disclosure,' there is an obligation 'to advise *correctly and completely*' * * * and any omission in explaining the Act [is] * * * a violation of the Act." (RAB 89) (emphasis respondent's) We find only that a consumer reporting agency violates Section 610 by advising consumers, expressly or implicitly, that disclosure cannot be obtained by telephone.

Congress has enacted a statutory scheme to remedy practices which were found to generate inaccuracy and unfairness in consumer credit reporting. The provisions concerning disclosure to the consumer contained in Section 610 of the FCRA are integral to the proper functioning of that congressional scheme. Respondent does not deny that had it acted directly to preclude consumers from exercising their rights under that section—specifically, their right to obtain telephone disclosure upon filing a written request—it would

have violated Section 610. We believe that the misrepresentations of respondent's employees that disclosure could only be obtained in person at a branch office (ID 563–65) amounted to refusals to make disclosure by telephone. As a direct consequence of these statements, some consumers abandoned their efforts to obtain disclosure by telephone and, instead, were left to seek disclosure by taking the time to visit one of respondent's offices. (ID 563, 566; Tr. 3481–82, 3578–79)

For consumers who are unable to visit one of respondent's offices, the adoption of respondent's construction of Section 610 would severely frustrate the fundamental purpose of the disclosure requirements, providing consumers a mechanism to discover, and correct, inaccurate information about them in a reporting agency's files. As noted earlier, Congress, in enacting the FCRA, was concerned both that access not be flatly denied, and that more subtle techniques not be employed to achieve the same end. Congress intended to prevent reporting agencies from building roadblocks between consumers and their credit files. We cannot permit Section 610, the statute's roadblock-clearing provision, to become a source of the very obstacles it was designed to eliminate. We, therefore, agree with the judge that to "foreclose telephone disclosure is tantamount to refusing it and violates Section 610 of FCRA." (ID p. 262)[60] [41]

Besides prohibiting respondent from misrepresenting to consumers their rights to disclosure under the FCRA, the ALJ ordered that when consumers make inquiry concerning disclosure, respondent advise them that they have the right to disclosure and tell them how to exercise that right. More specifically, the judge ordered that respondent inform consumers of the means by which they may obtain disclosure by telephone and supply any forms it requires consumers to execute to obtain disclosure.

Respondent challenged the breadth of the ALJ's prohibition against misrepresentations to consumers of their rights under Sections 609 and 610. We will instead prohibit only those misrepre-

[60] Respondent notes that, according to one of the commentators,

> while the FCRA is clearly a broadly remedial measure, it should be equally apparent that the Act is the product of compromise. Therefore, in interpreting the Act in marginal cases, one cannot rely, without question, on the principle of liberal construction. Rather it is necessary always to be aware of the definite and intended limitations in the FCRA's scope and effect.

Note, p. 28 *supra*, at 466 (footnote omitted). Nevertheless, whether or not the FCRA is provided the liberal construction normally accorded a remedial statute, *see SEC* v. *Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 195 (1963); *FTC* v. *Mandel Bros., Inc.*, 359 U.S. 385, 389 (1959), the character of the statute is such that we do not believe it should be construed so technically and restrictively as to eliminate the flexibility needed to effectuate its remedial purposes. The FCRA is designed to promote fairness, accuracy, and efficiency. In this case—which we by no means consider "marginal"—where the law creates a particular right, such as the right to receive telephone disclosure, we believe it must logically be read to preclude action that prevents the exercise of that right.

sentations demonstrated by this record, misrepresentations as to consumers' rights to obtain disclosure by telephone. Respondent has not questioned the propriety of the affirmative relief ordered by the judge. With some minor stylistic modifications, we will enter the affirmative order provisions which he proposed.

b. *Suboffice Disclosure*

Respondent concedes that it does not systematically provide disclosure at its suboffices (C. Ans. 26),[61] but the ALJ declined [42]to hold that this failure constitutes a violation of the FCRA. Suboffices are located within a branch office's territory, and, as the ALJ found, they "do not maintain full file storage systems and do not have full responsibility over their territories other than in producing reports * * * ." (ID 80) Complaint counsel, however, urge on appeal that since disclosure would be feasible at some of respondent's suboffices—those "staffed by at least one full time office employee and a person in a supervisory capacity" (CAB 19)—respondent must provide it at those offices to comply with Section 610. We do not agree.

Section 610 mandates disclosure "during normal business hours and on reasonable notice." It does not, however, expressly address the question of where, or at what level of a consumer reporting agency's organization, disclosures should occur. Judge von Brand made no findings to the effect that the absence of suboffice disclosure directly or indirectly foreclosed consumers from obtaining in-person disclosure, and we are aware of no basis in the record for such a conclusion. Moreover, we agree with the judge that respondent's organizational structure is not the source of the flaws in its disclosure practices. The purpose of the suboffice in respondent's organization is to provide a centralized "pied-a-terre" where a small number of field representatives can make and receive calls concerning their investigations and, in some cases, get clerical assistance.

The statute also provides for disclosure to be made on the telephone. We are satisfied that adherence to this statutory requirement together with systematic in-person disclosure at the branch offices is adequate to afford consumers the ready access to their files

[61] The judge found that

> [a] suboffice is generally removed from the metropolitan area, located in a small city or town. It is staffed by one or more field representatives, and, in the case of those having more than one field representative, one of them is designated as the supervisor. There may or may not be part-time or full-time clerical personnel. In some cases, the suboffice is located in the field representative's home * * * . The number of suboffices also varies from time to time. No files are maintained in suboffices.

ID 569 (citations omitted).

which Congress mandated, and that the ALJ was correct in refusing to add systematic suboffice disclosure to that mandate.

4. Reinvestigation of Disputed Information

Section 611 requires reporting agencies to reinvestigate information which is disputed by a consumer "unless it has reasonable [43] grounds to believe that the dispute by the consumer is frivolous or irrelevant." The reinvestigation must be conducted "within a reasonable period of time" and if, after the reinvestigation, the information is found to be inaccurate or can no longer be verified, the reporting agency must promptly delete the information. FCRA, Section 611(a). Section 611 includes several other protections, including a requirement that the reporting agency, at the request of the consumer, notify past recipients of the report that information has been deleted or notify them of the consumer's version of the dispute. FCRA, Section 611(d).[62]

Respondent provided its field management with detailed instructions on how to comply with Section 611. (ID 574–76) Despite these instructions, which were, for the most part, consistent with the statute, the record shows that, in a number of instances, respondent's employees have failed to reinvestigate items of disputed information.

The ALJ ordered respondent to cease and desist from failing to comply with Section 611's reinvestigation requirement but concluded that there were too few instances of violations of other requirements of the section to warrant imposition of an order prohibiting future infractions. Respondent appeals from the judge's findings that it has violated the reinvestigation requirement, and complaint counsel appeal from his failure to prohibit respondent from engaging in other violations of Section 611.

The ALJ found improper failures to reinvestigate in offices located in widely separated parts of the country.[63] Respondent acknowledges that it did not perform reinvestigations in three of the cases cited by

[62] Notifications need only be sent to persons who have received a consumer report for employment purposes within the past two years and persons who have received a consumer report for any other purposes within the past six months. FCRA, Section 611(d).

[63] We agree with the ALJ's determination that respondent failed to reinvestigate the disputed information cited in ID 578, although we differ somewhat with the ALJ's analysis. The record shows that the consumer disputed certain information in her report. (Tr. 1530, 8061) This witness, whom the ALJ found credible on this issue, also testified that while she was told by respondent's field representative that the information would be reinvestigated, subsequently, she was told when she "tried calling them back and nothing had happened as yet," (Tr. 1506) that "he would be in touch." (*Id.*) She went on to testify, "And I never did hear from him." (*Id.*) We assume the field representative's promise to "be in touch" was more than the classic "Don't call us, we'll call you" and that he intended to notify her on completion of the reinvestigation. The consumer's unrebutted testimony that she received no such notification, the absence of any explanation in this record of the failure to notify her, and the lack of any evidence that the promised reinvestigation was completed compels us to affirm the ALJ's determination that respondent breached its duty to reinvestigate.

the ALJ. It asserts, however, that in each of these instances, it was not required to reinvestigate, because it had reasonable grounds to believe that the dispute by the consumer was frivolous or irrelevant. (RAB 92) [44]

Equifax characterizes as frivolous a consumer's dispute as to a report it had prepared for an automobile insurer which concluded from information in the file that the consumer "shows a poor driving reputation in the area." (ID 581; CX 332A–B) The insurer had refused to issue a policy because of respondent's report, and the consumer had subsequently made two visits to respondent's office, during the course of which he disputed the information on which the conclusion had been based and furnished a list of references who, he believed, would attest to his good driving habits. Respondent first contends that the consumer's dispute was frivolous because on his first visit to respondent's office the consumer had not disputed certain adverse items in the report concerning his driving habits and, as to one item, had only raised an issue of "semantics," by challenging the report's conclusion that he was a bad driver. (RAB 92) The ALJ, however, correctly found that a factual dispute was clearly raised by the statement of dispute and reference list which, according to respondent, the consumer supplied at the second meeting. (ID 581 n.222) In any case, respondent failed to reinvestigate any of the disputed information, even that which the ALJ properly found the consumer had challenged at the first meeting.

Respondent also argues that the dispute was frivolous, and no investigation was necessary, because respondent had already interviewed two of the individuals on the consumer's list of references when it prepared the initial report. Section 611(a), however, provides that "[t]he presence of contradictory information in the consumer's file does not in and of itself constitute reasonable grounds for believing the dispute is frivolous or irrelevant." [45]

We are unconvinced by respondent's attempts to belittle the disputes of other consumers.[64] In our view, a reporting agency may

[64] Respondent characterizes another dispute as frivolous because the consumer asserted that everything in his file, except his name and address, was incorrect but refused to specify further the items he disputed. The ALJ found, however, that the consumer did specifically challenge certain items of information. (ID 579) In any case, at least where, as here, the file is not extensive, we cannot see how the dispute can properly be regarded as frivolous merely because the consumer asserts that everything in the file is inaccurate.

In such cases, the reporting agency may properly encourage consumers to identify the particular portions of their files which they dispute and point out to them that specific identification may help expedite the reinvestigation. Moreover, even if the consumer purports to dispute the entire file, the agency need not reinvestigate those items as to which it reasonably believes the disputes are frivolous or irrelevant. For example, this consumer's file included some information—such as the date on which the consumer was interviewed—about which any purported dispute was almost certainly irrelevant or frivolous. On the other hand, where the file is extensive and contains many items which could be disputed, it would not appear to be inconsistent with Section 611(a) for the agency to require that the consumer identify the items he or she disputes and conclude from the consumer's refusal to do so that the purported dispute is frivolous.

(Continued)

not properly conclude that a dispute is "irrelevant" [46]unless it can conclude that the disputed information is not adverse, that is, information which may have, or may reasonably be expected to have, an unfavorable bearing on a consumer's eligibility for credit, insurance, employment, or other benefit. *See* note 9 *supra.* A dispute over information which might reasonably be expected to harm a consumer simply cannot be "irrelevant."

Nor do we see how a reporting agency may properly conclude that a dispute is "frivolous" unless it is clearly "beyond credulity" or made in bad faith. *Cf. NLRB* v. *Lucy Ellen Candy Div. of F & F Laboratories, Inc.,* 517 F.2d 551, 555 (7th Cir. 1975); *Dickinson* v. *French,* 416 F. Supp. 429, 432 (S.D. Ala. 1976); *Boruski* v. *Stewart,* 381 F. Supp. 529, 533 (S.D.N.Y. 1974). Relevant factors under this standard include whether the dispute is repetitious of earlier disputes already reinvestigated, whether it is clear that reinvestigation would not reveal information contrary to that contained in the original report, or, perhaps, whether the dispute has been raised only for the purpose of harassment.

The statutory "frivolous or irrelevant" standard for dispensing with a reinvestigation may be seen as similar to that applied by the courts in deciding whether a claim need not be tried because there is "no genuine issue as to any material fact." As one court has put it, the standard must be met with such "clarity as to leave no room for controversy and that the other party is not entitled to recover under any discernible circumstances." *Nathanson* v. *United States,* No. 79–2013, slip op. at 8–9 (8th Cir. Aug. 12, 1980). In view of the importance of the reinvestigation requirement to the statutory scheme, the "frivolous or irrelevant" exception should also be construed sufficiently narrowly that doubts are resolved in favor of reinvestigation.

Respondent has also proposed that we read two more exceptions into Section 611. The ALJ properly found that, upon obtaining disclosure, a consumer disputed the accuracy of her report and also informed one of respondent's employees that she intended to undertake some follow-up research herself (ID 582)—a not unlikely reaction in light of the fact that she was not informed that a

Respondent justifies its failure to reinvestigate a third case because it deemed the disputed information to be irrelevant. After he was informed by his insurer that his premiums were being increased on the basis of a report supplied by respondent (Tr. 3142), the consumer obtained disclosure of his report and disputed two items concerning his financial affairs. (ID 580) Respondent asserts that its office manager had reasonable ground to believe that the insurance premiums were being increased because of other information in the report which the consumer did not dispute. (RRB 42) Respondent's duty to reinvestigate, however, was not limited to information it reasonably believed to be relevant to the denial of a particular benefit. The report labeled the consumer's "finances" as a "significant" feature. (CX 138A) As long as it remained in the consumer's file, the information could be used by another customer to deny a benefit, and, therefore, should have been reinvestigated.

reinvestigation would be conducted. (*Id.*) Respondent argues that "it was reasonable to defer any action on reinvestigation until [the consumer] returned or responded." (RAB 92) The statute, however, requires that the reporting agency *promptly* reinvestigate disputed information unless the dispute is irrelevant or frivolous. Reporting agencies, not consumers, are responsible for reinvestigations and, accordingly, may not avoid, or postpone, conducting reinvestigations on the expectation that consumers will do their work for them.

In another instance, respondent claims that it was under no duty to reinvestigate because the consumer had stated that he intended to sue. Respondent argues that it "can certainly conclude that a consumer has waived his right to a reinvestigation * * * when the consumer states that he is going to sue." (RAB 93) **[47]**Even assuming the statute permits the consumer to waive a reinvestigation of disputed information, respondent has not explained why a threat to litigate would amount to a waiver, as opposed to a forceful assertion of the consumer's right to have challenged information reinvestigated and corrected. Nor do we believe that the prospect of litigation renders a reinvestigation pointless, as asserted by respondent. Although the purpose of a reinvestigation is clearly to resolve the differences between the consumer's understanding of the facts and those contained in the file, we cannot agree that "[i]f the consumer is going to sue in any event, conducting a reinvestigation is 'baseless' since the consumer has made it clear that the dispute cannot be resolved in that manner and the reinvestigation would be purely an academic exercise." (RRB 42) The statutory purpose of the reinvestigation requirement is to encourage the correction of errors rather than to discourage litigation, and the reporting agency's ability to remedy error is not foreclosed by the prospect of litigation concerning the accuracy of the file.

We are not persuaded by complaint counsel that we should broaden the ALJ's order to prohibit violations of Section 611 other than failures to reinvestigate.

C. Reporting of Obsolete Adverse Information

Section 605 of the FCRA generally prohibits consumer reporting agencies from reporting any "adverse item of information which antedates the report by more than seven years." This prohibition reflects a determination by Congress that it would be "unfair to burden a consumer for life" with adverse information when the consumer "has improved his performance." S. Rep. 91–517, *supra*, at

4. The complaint alleges that Equifax has violated Section 605 by its use of the following "stock sentence" in certain employment reports:

> In compliance with the Fair Credit Reporting Act, no additional information can be reported from this former employer covering employment experience prior to seven years ago.

Complaint, ¶ 18(1). Respondent has stipulated that it is a "matter of established procedure" to include this stock sentence in reports, or otherwise to indicate that the FCRA does not permit the reporting of "such" information, "when respondent obtains adverse information more than seven years old from a former employer * * * ." (CX 1445D) The stock language is *not* used if no obsolete adverse information is discovered. (ID 272) The ALJ found that this selective use of the stock sentence serves to "signal the existence of adverse information in violation of Section 605." (ID p. 229; *see* ID 272.) We affirm.

Respondent does not assert that Section 605 prohibits only the reporting of specific items of information. Such a reading of the [48] statute, which would be consistent with ratifying the selective use of the stock sentence, would produce an absurd result. As the judge pointed out, it would effectively preclude the consumer from taking advantage of the disclosure requirements of the Act and to challenge the items with which he or she disagrees. (ID p. 230) However, even though respondent does not make that assertion, it does challenge the judge's finding of a violation on the ground that the sentence does not, necessarily, indicate the existence of obsolete adverse information.

It is clear, under the circumstances, that use of the stock sentence signifies that the file contains adverse information.[65] We are not persuaded by respondent's argument that a violation depends on evidence that employers actually interpret the stock sentence to suggest the existence of adverse information that is over seven years old, since we agree with the ALJ that it would be difficult to interpret the sentence otherwise. Respondent further argues that this position "ignore[s] the thrust of [its] contention" that "[a]n 'item of information' is not 'adverse' (within the meaning of FCRA Section 605(a)(6)) unless likely to cause adverse action." (RRB 23) We agree with respondent's characterization of "adverse information" and have adopted, in essence, the definition of "adverse information"

[65] Respondent argues that a report that contains no mention of the obsolete information is an "artfully ambiguous report[] that seek[s] to conceal the existence of unfavorable data." (RAB 52) Respondent, however, could simply inform its customers generally of the limitations imposed by Section 605 or could include the boilerplate in all its reports with an appropriate explanation that no inference should be drawn from the language as to the existence of adverse information in the file.

contained in respondent's proposed findings. *See* note 9 *supra;* RPF 1(h). Regardless of how adverse information is defined, however, respondent effectively admits that the rationale for its use of the boilerplate language is to communicate to the user of the report that the consumer's file contains information which respondent believes falls within the scope of Section 605(a)(6) as being both adverse and obsolete and which respondent believes it cannot disclose under the terms of that section. (RAB 52)

Finally, respondent challenges the scope of the judge's order which bans all violations of Section 605. The ALJ found no violations of Section 605 other than the "signaling" of obsolete adverse information by selective use of the stock sentence. There is no evidence in this record that respondent has included obsolete adverse information, except for its use of the boilerplate language, and we are unaware of anything in the record which would otherwise [49] support the need for "fencing-in" relief.[66] Accordingly, we modify the order to preclude respondent from signaling the existence of obsolete adverse information by indicating in employment reports directly or indirectly, through use of a "stock sentence" such as the one shown on the record, the existence of adverse information which antedates the report by more than the applicable period of time specified in Section 605.[67]

D. Use of Consumer Reports for Permissible Purposes

The FCRA is intended not only to ensure the accuracy of consumer reports but also to protect the individual consumer's right to privacy. This latter purpose is articulated in Section 602(a):

> There is a need to insure that consumer reporting agencies exercise their grave responsibilities with fairness, impartiality, and a respect for the consumer's right to privacy.

The most important of the sections promoting the privacy of individual consumers is Section 604, which severely restricts the circumstances under which consumer reporting agencies may disclose consumer reports to third parties.[68] The complaint alleges that respondent has violated this section by providing its customers with

[66] Complaint counsel did not appeal from the ALJ's rejection of the complaint allegation that respondent violated Section 605 by "furnishing * * * photocopies of motor vehicle reports reflecting masked out or obliterated driving violations which antedate the report by more than seven years, but which indicate the existence of said obsolete violations." (Complaint, ¶ 18(2))

[67] If respondent chooses to use a stock sentence, it will be required to include an explanation that the language is used regardless of whether obsolete information was discovered. This explanation will be necessary to dispel the inference which customers will continue to draw absent an explanation, that use of the sentence signifies the presence of adverse information.

[68] *See* note 2 *supra.*

what it terms a "Voluntary Follow-Up Service." According to the complaint, through this and other similar services, respondent, on an unsolicited basis, submits to customers adverse information about consumers as to whom previous reports have been furnished, even though "respondent has no reason to [50]believe that it will be used in connection with a business transaction such as the underwriting of insurance." (Complaint, ¶ 16)

The complaint also alleges that, as a result of the manner in which information contained in claim reports and consumer reports is interchanged, respondent disseminates consumer reports in violation of the requirements of this section. (Complaint, ¶¶ 28, 29)

1. Voluntary Follow-Up Service and Monetary Savings Plan

a. *Voluntary Follow-Up Service*

Until April 1974, respondent routinely furnished its customers follow-up information on consumers about whom it had already furnished a consumer report.[69] Under this "Voluntary Follow-Up Service," subsequently developed adverse information was supplied to update a consumer report which had not identified a "risk or hazard." (ID 264 n.87) The complaint alleged, and the ALJ found, that the subsequent information constituted consumer reports which respondent did not have reason to believe would be used for a Section 604 permissible purpose. We agree.

Respondent does not dispute that the Voluntary Follow-Up Service reports were consumer reports. It does contend, however, that it reasonably believed that the recipients of the information would use it for a permissible purpose.

The parties and the ALJ seem to agree that the customer—in each case an insurance company—could use the supplemental information for a permissible purpose if the insurer had a policy in effect with the consumer who was the subject of the report.[70] Moreover, the insurance company could clearly put the information to a permissible use if, at the time it received the follow-up report, it had not yet acted on the insurance application.

From this, respondent argues in its appeal that

> [i]n light of the fact that the vast majority of report subjects do in fact qualify for and receive insurance from the company that has [51]ordered a report * * * and the further fact that voluntary information was reported only shortly after the furnishing

[69] Respondent discontinued this service two months after issuance of the instant complaint. Respondent's decision to terminate the service was based, according to its Senior Vice President, "to some extent" on the pendency of the complaint. (Tr. 5187–88) *See* pp. 77–78 *infra*.

[70] The information might trigger an investigation by the insurer to determine whether the policy should be rescinded. (Tr. 2678)

of the original report * * *, respondent surely had a reasonable basis for believing that the report was being forwarded for a permissible purpose.
RAB 48.

We take this as a concession that in *some* cases the recipient of the report would not have a policy in force at the time it received the follow-up information.[71] Nor do we understand respondent to contend that in *every* case in which a policy was not in effect, the recipient had yet to act on the consumer's application. Indeed, the record shows that follow-up information was sometimes transmitted a substantial time (up to 90 days or more) after the sending of the initial consumer report.[72] [52]

The essence of respondent's argument, however, is that it had "reason to believe" the information would be used for a permissible purpose because, in *most* cases, the insurance company either could be expected to use the information to determine whether to grant a pending application (the application which triggered the initial consumer report) or had an insurance policy in force with the subject of the follow-up report. We reject respondent's understanding of its obligation. The consumer reporting agency's belief that a report will be used for a permissible purpose must be based on what it can reasonably conclude the particular customer will do with the specific information. Section 607(a) provides:

Every consumer reporting agency shall maintain reasonable procedures designed to * * * limit the furnishing of consumer reports to the purposes listed under section 604. These procedures shall require that prospective users of the information identify themselves, certify the purposes for which the information is sought, and certify that the information will be used for no other purpose.

These requirements, designed to prevent violations of Section 604,

[71] Indeed, in its proposed findings of fact, respondent stated:

Insurance companies who received voluntary information sometimes had a policy in force in connection with the individual who was the subject of the voluntary follow-up *and other times did not.* * * * When the companies did not have an insurance policy in force on an individual, the information was placed in an inactive file or simply discarded.

RPF 245 (citations omitted) (emphasis added).

[72] One of respondent's instruction manuals advised field representatives that

[i]f, within 90 days from the date a [life] report is submitted, protective information comes to our attention that might have a definite bearing on the subject's insurability, the customer should be notified by wire. If more than 90 days have elapsed, then the Voluntary Information Report, Form 121, should be used.

CX 667Z-29.

Whether or not, as respondent claims, field representatives submitted information for voluntary follow-up purposes only to management personnel, who would decide whether to send the information to the customer (RRB 18), the manual makes it clear that it was company policy to forward voluntary information as much as 90 days after an original report was submitted to the customer.

Other testimony indicates that voluntary follow-up information was transmitted as long as six months after the original report. *See* Tr. 4665, 5784–85.

assure that the reporting agency will have at least some information about how the particular customer will use the information which it seeks.[73] These safeguards would make no sense if a reporting agency could satisfy its obligation under Section 604 by assuming that, because most customers use such information for a permissible purpose, so will any particular customer to which it proposes to send a consumer report.

b. *Monetary Savings Plan*

Complaint counsel have challenged another program by which respondent supplies unsolicited information about consumers to the insurance companies who purchase its consumer reports. Equifax calls this program, which was still in use at the time the record [53] closed, its Monetary Savings Plan. Under this program, respondent's sales force transmits to customers information about the subject of a previously prepared consumer report. This may be done if respondent discovers that an event has occurred which would cause an insurance company a loss and the initial report would have permitted the insurance company to identify the risk and either rate or decline the application. The parties agree that this additional information has been supplied as a sales tool to demonstrate the value of respondent's reporting service. The ALJ also found that these follow-up reports are "consumer reports" and that respondent has violated the statute by furnishing them to persons whom it has no reason to believe intend to use the information for one of the permissible purposes set out in Section 604.

The threshold question is whether the Monetary Savings Plan reports are "consumer reports" within the meaning of Section 603(d), since it is only the furnishing of consumer reports for impermissible purposes that is prohibited by Section 604. A consumer report is a communication bearing on any of the seven criteria listed in Section 603(d) "which is used or expected to be used or collected in whole or in part for" any of the purposes listed in Section 603(d) or Section 604. *See* note 1 *supra.* Thus, as we noted in *Howard Enterprises, Inc.,* 93 F.T.C. 909 (1979), Section 604 serves two functions, the primary one being to establish the permissible uses of consumer reports, and the second, to add content to the Section 603(d) definition of a consumer report. We also held that a report of information "is used or expected to be used" for one of the purposes enumerated in Sections 603(d) and 604 so long as it "could be used"

[73] The complaint did not allege, and complaint counsel do not assert, that respondent has failed to comply with § 607(a) by failing to obtain the certifications prescribed by that section. We, therefore, do not find that any failures to obtain certifications were, in themselves, violations of the statute.

for one of those purposes. *Id.* at 933 n.9. *See also Belshaw* v. *Credit Bureau of Prescott,* 392 F. Supp. 1356, 1359-60 (D. Ariz. 1975). Finally, we held that the residual category of permissible uses included in Section 604—use by a person whom the reporting agency has reason to believe "otherwise has a legitimate business need for the information in connection with a business transaction involving the consumer"—is limited to business transactions "between report users and consumers acting as consumers." 93 F.T.C. at 933 n.5.

Use of information by customers to assess the value of respondent's services is clearly not one of the permissible uses listed in Sections 603(d) and 604. It does not follow, however, that Monetary Savings Plan reports are not consumer reports within the meaning of Section 604. Even though these reports were not disseminated for one of the permissible purposes, they were consumer reports so long as they included information which was either "collected in whole or in part," or which could be used by the recipient, for one of the permissible purposes.

The record shows that Monetary Savings Plan reports at times include information falling squarely within the definition of a consumer report. Respondent's Senior Vice President testified that Monetary Savings information would include information subsequently [54]developed for "the same type of report" as that originally furnished the customer. (Tr. 5237) Respondent's Executive Vice President likewise testified that the company would supply information developed by a field representative during a subsequent investigation in connection with a "different" report. (Tr. 5855)[74] Consumer reports, that is, reports which are "used or expected to be used or collected in whole or in part" for one customer for one of the statutory purposes, do not lose their status as consumer reports once they are communicated to another customer for some other purpose. If they did, Section 604 would be drained of all meaning. Therefore, because the Monetary Savings Plan reports are consumer reports their dissemination for other than a permissible purpose violates Section 604.

c. *Order*

Because of the limited nature of the violations we have found — furnishing information to prior recipients of consumer reports who presumably once had a permissible purpose for receiving the information —we agree with respondent that the ALJ's order should

[74] The witness was clearly referring to an investigation leading to a consumer report which had been requested by a different insurance company.

be narrowed. Rather than prohibiting respondent from submitting consumer report information to any person it lacks reason to believe will use the information for one of the permissible purposes, we will prohibit respondent from transmitting updated consumer report information to customers which have received a previous report concerning the same consumer except under the circumstances listed in Section 604.[75]

We will also delete the ALJ's requirement that respondent first obtain a specific request for a follow-up disclosure. Depending on how it is worded, the certification of purposes from the customer required by Section 607(a) may be broad enough to encompass follow-up information.

The certification, however, will not necessarily provide respondent "reason to believe" that the customer intends to use particular follow-up information for a permissible purpose. Respondent's Executive Vice President acknowledged that Equifax "has no way to determine [how long it takes an insurance company to underwrite a policy] because I would guess their work load and their systems and so forth would vary from one customer to another and it would take one company longer than another." (Tr. 5855) In some cases [55] respondent may be able reasonably to assume that customers will use for a permissible purpose a follow-up report supplied a few days after the original report was sent. The assumptions respondent may reasonably make will depend on the circumstances of the case and its knowledge of the user's practices. Our order will only require that respondent, before sending such follow-up information, have reason to believe that the customer intends to use it for a permissible purpose as set out in Section 604. Respondent may be able to obtain this reason to believe simply by inquiring of the customer how soon it intends to act on the application or whether, before acting, it will await the follow-up report. Respondent might also have reliable general knowledge of the time it takes a certain customer to act on an application, once the customer has received an initial report from respondent.

Finally, respondent asserts that a prohibition against its disseminating "information obtained from newspapers or public records" would violate the First Amendment. (RAB 51 n.48) However, circulation of these items of information would be prohibited by our order only if they are consumer reports within the meaning of Section 603(d). Respondent contends, and it appears from the record, that they are not. We are unaware of any evidence which contradicts

[75] As modified, the order permits disclosure under any of the circumstances listed in the section, rather than only the circumstances listed in Section 604(3).

respondent's assertion that the news clippings and other public record information disseminated in this program are not "used or expected to be used or collected in whole or in part"[76] for one of the permissible purposes listed in Section 604. FCRA, Section 603(d).

2. Interchange of Information between Claim Reports and Consumer Reports

The complaint alleged that in the preparation of its consumer reports and claim reports, respondent uses all of its file information interchangeably—it uses claim report information in the preparation of its consumer reports and consumer report information in the preparation of its claim reports. The complaint further charged that, by these practices, respondent has failed to comply with various provisions of the FCRA governing the preparation and dissemination of information which is used or expected to be used in consumer reports. (Complaint, ¶¶ 28 and 29) During the course of the trial, complaint counsel sought to establish that claim [56]reports *become* consumer reports when they are used or are available for use in preparing consumer reports and that they are, accordingly, subject to all the requirements of the FCRA pertaining to consumer reports. The judge rejected this latter contention, and complaint counsel do not appeal from the ALJ's determination.

Instead, the ALJ held that Section 604 does not permit the use of consumer report information in the preparation of claim reports. Respondent's challenge to the ruling is limited, principally, to a contention that this theory of violation was not properly before the ALJ. (RAB 94–95) We are doubtful about the validity of the theory relied on by the ALJ and neither of the parties has adequately briefed the issue. We also do not believe that the public interest would be served by an order about which we entertain substantial doubt. Rather than requesting further briefing, we conclude that the public interest would best be served by our setting aside the ALJ's findings on this issue.

IV. Section 5 Charges

A violation of any requirement or prohibition imposed by the FCRA and enforced by the Commission constitutes an unfair or deceptive act or practice in violation of Section 5 of the FTC Act.

[76] Although employees were instructed to place newspaper clippings in the files (CX 1365Z–25), it does not follow that the clippings which have been transmitted as part of the Monetary Savings Plan are "used or expected to be used or collected in whole or in part for" the purposes enumerated in Sections 603(d) and 604.

We are not persuaded that follow-up information is necessarily a consumer report merely because it is relevant to a customer's assessment of the value of a consumer report. (ID p. 226)

FCRA, Section 621(a). The complaint in this case also challenged as violations of Section 5 several alleged practices which the FCRA does not address.

A. Misrepresentations of Identity in Preparation of Consumer Reports

The complaint alleged that respondent's investigators have represented to those whom they interview, directly or by implication, that "they are agents or employees of the company to which the consumer has applied for a benefit, such as insurance * * * and/or [that] the information furnished by the consumer or others during an interview, will be used exclusively by the company to which the consumer has applied for a benefit * * * ." These practices, the complaint alleged, are "unfair, false, misleading and deceptive in violation of Section 5 of the Federal Trade Commission Act." (Complaint, ¶¶ 5, 6)

The judge found that, in practice, respondent's employees did not always identify themselves as being employees of Retail Credit, in large part, because the company name "sometimes confused consumers and led to the impression that credit rather than insurance was the reason for the investigation."[77] (ID 160-61; [57]ID p.216 n.227) Instead, according to the judge, field representatives identified themselves to consumers by stating that they were "from," "with," "calling for" or "conducting an investigation for" the insurance company or other customer of respondent who had requested the report, or that the interview was in connection with a particular insurance application. (ID 162)[78]

The judge reasoned:

> An introduction by a field representative stating that he was "from" or making contact "for" an insurance company, that he was calling in connection with an insurance application or a similar introduction unaccompanied by the disclosure that he worked for Retail, had the tendency to create the impression that the field representative was an insurance company employee or agent rather than the employee of a third party consumer reporting agency.
>
> ID 163.

[77] There is also testimony on the record that, when respondent's field representatives did not volunteer that they were employed by Retail Credit at the start of an interview, if pressed by the consumer for further identification, they eventually gave Retail Credit's name and sometimes produced company identification cards.

[78] Prior to amendments made in 1973, the company's Field Representative Manual stated that the name Retail Credit should be used when interviewing the subject of a report, but also suggested that when the requesting company desired use of its name in the introduction, then "the Field Representative should state that he is 'calling for the X Insurance Company.'" (ID 159) The ALJ correctly determined that this introduction "would misrepresent, by implication, the identity of the caller if Retail Credit were not mentioned." (ID 159 n.54) The 1973 Manual instructed field representatives to state their names and Retail Credit's name when interviewing the subject of the report and both permitted and encouraged them to mention the name of the company requesting the report. (ID 158)

The judge also determined that the identity of the interviewer is material to the consumer. He based this determination on the testimony of several consumers who either refused to answer the interviewer's questions when they were eventually told that the interviewer was a field representative of Retail Credit Company rather than an employee or agent of the insurance [58]company. In addition, he cited the testimony of one witness who might not have answered the questions had the interviewer's true identity been revealed. (ID 164)

The ALJ also found that respondent's field representatives have misrepresented the use to which the information they sought would be put: that is, their actions implied that the information would be used only by the customer, rather than being retained by respondent for future use. However, he determined that this misrepresentation was implicit in the field representatives' misrepresentations of identity and did not premise his finding simply on "respondent's failure to affirmatively disclose to consumers that it keeps a file copy [of the report] and may subsequently use it." (ID 165 & n.57) Accordingly, the order provisions only prohibit respondent from representing, directly or by implication, that its investigative personnel are agents or employees of the company to which the consumer who is the subject of the report has applied for a benefit.

We affirm the ALJ's findings and his order, as well.

Evidence of actual deception is not necessary to finding a violation of Section 5. It is well settled that only the "capacity to deceive need be shown." *Trans World Accounts, Inc., supra; Charles of the Ritz Distributors Corp.* v. *FTC,* 143 F.2d 676 (2d Cir. 1944); *see FTC* v. *Raladam Co.,* 316 U.S. 149 (1942).

In determining whether deception exists, the Commission may rely upon its own first-hand evaluation of the evidence. *Carter Products, Inc.* v. *FTC,* 323 F.2d 523, 528 (5th Cir. 1963); *see FTC* v. *Colgate-Palmolive Co.,* 380 U.S. 374, 391-92 (1965); *ITT Continental Baking Co., Inc.,* 83 F.T.C. 865, 954 (1973), *modified,* 532 F.2d 207 (2d Cir. 1976). "The Commission has the discretion to interpret the meanings of various communications and 'the impressions they would likely make upon the viewing public' * * * [and] [t]he Commission may draw its own inferences regarding the likelihood of deception based upon the representations before it." *Trans World Accounts, Inc.* v. *FTC, supra,* 594 F.2d at 214; *see also Libbey-Owens-Ford Glass Co.* v. *FTC,* 352 F.2d 415, 417 (6th Cir. 1965); *Stauffer Laboratories, Inc.* v. *FTC,* 343 F.2d 75, 78 (9th Cir. 1965).[79] We agree

[79] Respondent argues that we should, nevertheless, follow the course we took in *Leonard F. Porter, Inc.,* 88

(Continued)

with Judge von [59]Brand that the failure of field representatives to identify Retail Credit as their employer combined with their assertions that the inquiries are "for" or "on behalf of" the insurance company had the tendency or capacity to deceive.

Respondent's objection to the judge's findings—that the initial decision "does not establish by the preponderance of the evidence that the alleged failure of field representatives to identify respondent as their employer is material" (RAB 13)—is without merit. Materiality is a matter which the Commission in its expertise may infer. *FTC* v. *Colgate-Palmolive, supra,* 380 U.S. at 392. We do not find it surprising that many consumers would be less willing to answer a question if they believed that the information were going to be made available for a variety of uses, in connection with insurance, credit, and employment applications, than they would if they believed the information would be used in connection with a single insurance application.[80]

Respondent also challenges the ALJ's finding "that respondent misrepresents by implication the use to be made of information which it obtains during interviews when field representatives fail to disclose the identity of their employer * * * even though there is *no* evidence that any field representative employed by respondent ever made an affirmative misrepresentation that respondent does not keep a file copy of the report." (RAB 14) Respondent asserts that this finding erroneously assumes that

> the average consumer is not only mistrustful; he or she is *selectively* mistrustful. He or she [60]supposedly believes that respondent is riddled with dishonest employees and is prone to disobey its legal obligations under Section 604 of the FCRA; yet he or she also believes that insurance companies not only are the epitome of discretion and integrity but will never have any occasion to disclose the information to others.

RAB 14–15 n.10 (emphasis in original).

We agree with the judge that at least some consumers who are informed that they are being interviewed by someone "calling on behalf of" an insurance company will likely be misled, as well, into

F.T.C. 546 (1976). In that case, the Commission held that testimonial evidence by consumers was needed because the Commission could not otherwise conclude whether respondent's practices had the capacity to deceive. This case, however, raises no such unusual problems. It takes no further evidence to demonstrate that a statement by some unknown caller to the effect that he or she is "calling for the X Insurance Company," without any mention of the person's employer—Retail Credit—would have the capacity to mislead the consumer into believing that the caller was, indeed, "from" or "employed by" the insurance company. The existence of corroborating evidence, such as the consumer testimony here, merely strengthens our conclusion, and the respondent's argument that the evidence is not overwhelming in quantity is irrelevant.

[80] Respondent notes that a number of present and former field representatives testified that they could not recall ever having been asked by an applicant or outside source if respondent maintained file copies of reports. (*E.g.,* Tr. 359–60, 12929, 13175–76; RPF 132(b)) However, other field representatives testified that consumers did ask them whether reports were retained (Tr. 9183, 12454; RPF 132(c)), and more might have expressed interest if they had not been led to believe that it was a single insurance company which was seeking the information.

believing the information which they supply will be used solely by that insurance company. Respondent, on the other hand, is in the business of collecting and reporting information about consumers for a variety of customers and, unlike an insurance company, can be expected to—and does—retain information collected for one customer for use in reports ordered by other customers.

We also note that, according to the ALJ,

> [t]o a considerable degree, the failure by respondent's personnel to identify themselves was occasioned by the confusion engendered by the name Retail Credit when the interview was in connection with an insurance investigation not involving credit, *e.g.*, insurance. To avoid the requisite explanations, respondent's field representatives would omit the name of their employer. The incentive to engage in such practices has been reduced by respondent's name change to Equifax (Findings 160–61).

ID p. 216 n.227. Respondent argues that "the alleged potential for confusion in the name 'Retail Credit Company' served as the foundation for all of the findings and the rationale of the Administrative Law Judge with respect to paragraphs 5 and 6 of the complaint," and that "[w]ith the abandonment of this name by respondent, the evidentiary basis and the process of reasoning employed by the Administrative Law Judge can have no continued validity." (RRB 5) If we were persuaded that the only reason for the misrepresentations was the possible confusion inherent in the name Retail Credit Company, we would be inclined to doubt the continued existence of a "cognizable danger of recurrent violation of Section 5" under the standard set out in *Kraftco Corp.*, 92 F.T.C. 416 (1978), *aff'd sub nom. SCM Corp.* v. *FTC*, 612 F.2d 707, 708 (2d Cir.), *cert. denied*, 49 U.S.L.W. 3245 (October 6, 1980).

The deceptions, however, in at least some instances, went far beyond anything needed to alleviate confusion over respondent's name—confusion, we might add, which respondent was not at all eager to avoid in its conduct of the indirect interviews [61]described below. We, therefore, conclude that, even with the abandonment of the name Retail Credit Company, there remains a cognizable danger of recurrence of the violation.

Finally, principally in connection with this complaint allegation, respondent argues that the FCRA limits the scope of Section 5 with respect to consumer reporting agencies. In this regard, respondent asserts:

> The procedures utilized by consumer reporting agencies with respect to the acquisition, retention and use of file information have been sanctioned and regulated by Congress through the FCRA and cannot constitute an unfair trade practice under Section 5, absent a violation of the provisions of the FCRA or absent an affirmative misrepresentation.

RAB 17 (footnote omitted).

Respondent notes that its challenge extends "only to those paragraphs of Count I [of the complaint] directed to the acquisition, retention, and use of information by respondent, matters that have been specifically considered by Congress and regulated in the FCRA." (RAB 17 n.12) Respondent states further that while the FCRA does not preclude all applications of Section 5 to consumer reporting agencies, it does preclude all such applications "[w]ith regard to issues that were * * * brought to Congress' attention during deliberations on the FCRA * * * ." (RAB 21) Finally, however, having said all of the above, respondent seems to limit its preemption argument to "two issues that have overriding importance in connection with assumptions underlying the Initial Decision: (a) the extent to which fairness precludes the very act of retaining information about consumers for later use; and (b) the extent to which fairness requires that consumers be given advance notice that the information they reveal will be acquired and retained by a reporting agency." (RAB 21) As to those issues, respondent claims that "the FCRA and the FTC Act are definitely *in pari materia* and the later, more specific enactment is controlling." (RAB 21)

We have not found that any practices sanctioned or even addressed by the FCRA violate Section 5. Rather, we have found that certain practices not treated in the FCRA have the capacity to mislead. As respondent points out, the FCRA effectively recognizes the validity of consumer reporting agencies' use of certain types of procedures in connection with consumer reports (*e.g.*, interviews and retention and reuse of information). Respondent, however, does not explain why the fact that Congress has enacted some provisions concerning acquisition, retention and use of information by consumer reporting agencies immunizes from Section 5 all other related practices. [62]

There is no evidence that Congress, in enacting the FCRA, intended to immunize the kinds of unfair or deceptive practices at issue in this case. *See generally L. Heller & Son, Inc.* v. *FTC,* 191 F.2d 954, 956–57 (7th Cir. 1951); *Perpetual Federal Savings and Loan Ass'n,* 90 F.T.C. 608, 656 n.14 (1977). Nowhere does the statute or its legislative history suggest an intent to condone deceptive practices in connection with the sanctioned activities of a consumer reporting agency. Respondent concedes that the FCRA does not preclude all possible applications of Section 5 to consumer reporting agencies, and it concedes, as well, that Section 5 reaches "affirmative" misrepresentations. (RAB 17 & n.12) We can see no justification for

336-345 O - 81 - 70

respondent's distinction between "affirmative" and implied misrepresentations, as both are reached by Section 5.

Even if, however, respondent's distinction were adopted here, this record contains evidence of "affirmative" misrepresentations sufficient to meet respondent's test. In any case, we do not premise our findings on either of the theories which respondent claims is foreclosed by the FCRA: "the very act of retaining information about consumers for later use" or the failure to provide consumers with "advance notice that the information they reveal will be acquired and retained by a reporting agency" is unfair. We simply find that in conducting its activities as a consumer reporting agency, respondent has engaged in a practice which deceives or has the capacity to deceive the consumer, and which, therefore, violates Section 5.[81]

We believe that the violation will be cured by a simple provision prohibiting respondent's field representatives from misrepresenting directly or by implication that they are agents or employees [63]of the company to which the consumer who is the subject of the report has applied for a benefit. There is no evidence to suggest that if Equifax employees comply with the order as proposed by the judge, their actions will have a tendency to mislead consumers either as to their identity and that of their employer or as to the intended use to be made of the information.[82] We therefore see no need for the additional prohibitions and affirmative disclosures proposed by complaint counsel. [64]

B. Indirect Interviews and Misleading Medical Information Authorizations

The judge sustained the complaint allegations that (1) respondent's investigative personnel, in the course of preparing claim

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[81] Respondent also argues that "[t]he *in pari materia* principle dictates that, in the instant case, the FTC Act must not be interpreted without regard for the lines Congress drew when it passed the FCRA, *particularly in a situation where Congress declined to provide the Commission with the power to issue regulations having the force and effect of law* [footnote omitted]." (RAB 20) (emphasis in original) As we have already stated, however, Congress had indicated no intent to condone or immunize from Section 5 deceptive practices in connection with the other legitimate activities of a consumer reporting agency. Moreover, regardless of whatever authority the Commission may have to promulgate trade regulation rules under Section 5 covering the credit reporting industry, here, we are simply construing the FTC Act in the course of an adjudication.

[82] Complaint counsel urge us to go beyond the findings of the ALJ and to determine that, wholly apart from the misrepresentations of identity, respondent's "failure to disclose to consumers that [it] will retain information for future reference has the tendency to mislead consumers as to a material fact." (CRB 19) Therefore, they argue, the Commission should order respondent affirmatively to disclose "not only its identity, but also the nature of its operation and its practice of retaining file copies of reports for future reference * * *." (CRB 21)

As noted in the text, the ALJ correctly found that "[t]he record fails to show that respondent affirmatively misrepresented that it did not keep file copies of the reports or that information furnished during an interview would be used exclusively by the company to which the consumer had applied for a benefit such as insurance." (ID p. 215) Complaint counsel have not shown that, absent the misrepresentations of identity which our order will prohibit, the failure of respondent to make affirmative disclosure as to the retention and future use of the information gained from interviews by its field staff would render the interviews deceptive under Section 5.

reports, have used deception to induce claimants to participate in interviews; and (2) respondent has obtained medical information about consumers from physicians and other medical personnel without proper authorization. Although he found that both practices violate Section 5, he determined that changes in respondent's procedures have obviated the need for an order addressed to the latter practice and that, in any case, the McCarran-Ferguson Act bars the Commission from ordering any relief.[83]

Respondent appeals from the findings that it has violated Section 5, and complaint counsel appeal from the judge's failure to order respondent to cease and desist from using the challenged procedures in the future.

1. The Indirect Interview

Until 1966, respondent instructed its employees to use a "pretext" in their attempts to obtain information from third-party claimants, that is, persons filing a claim against someone else's insurance company. Investigators might, for example, represent to the claimant that they were "looking for a person [they] believe[d] that resided in the neighborhood, [and ask whether the claimant] had ever heard of that person." (ID 168 & n.59) The primary purpose of these contacts was to afford the field representative an opportunity to observe the physical condition of consumers who had filed claims for personal injuries. The pretext was designed to encourage individuals who might otherwise be uncooperative to participate in the interview and, of course, permit respondent's employees to observe their condition. Respondent does not challenge the ALJ's findings that these procedures were unfair or deceptive (ID 167–75),[84] and we affirm those findings.

In 1966 and, again, in 1971, respondent modified its method of obtaining information from third-party claimants. Field representatives were instructed in 1966 to "give the name 'Retail Credit [65] Company' and indicate that [they were] making inquiry, ostensibly for credit purposes." (RX 651A) They were to complete a form bearing the title "Credit File Audit" (RX 651B), which "was designed so that when seen by the interviewee * * * it would give the impression that the investigation being conducted was a credit investigation * * * ." (ID 172) In 1971, respondent replaced the "Credit File Audit" form with a "Personal Interview" form (RX

[83] Respondent has raised the McCarran-Ferguson Act exemption only with respect to these two alleged violations.

[84] We also understand respondent to acknowledge that misrepresentations were made in connection with the procedure used until 1971 (the "Credit File Audit" approach) (RAB 23 n.22), despite its assertion that this interview technique did not violate Section 5 standards. (RAB 22 n.21)

575C), which the claimant was allowed to "handle * * * if he [were] so inclined." (RX 119V) If the claimant asked the field representative the purpose of the interview, the representative was to state that he or she was not permitted to divulge the purpose or the source of the request. Employees were instructed that "[i]t is imperative that our approach not include any misrepresentation." (ID 176)

The ALJ correctly decided that the changes initiated in 1966 and 1971 did not strip the indirect interviewing technique of its deceptiveness. The 1966 procedure clearly involved representations to claimants that credit checks, rather than claim investigations, were being conducted. The 1971 procedure involved more subtle misrepresentations of the purpose of the investigations.

The ALJ found that the "Personal Interview" approach, "while not involving affirmative misrepresentations," when used in conjunction with the Retail Credit Company name, "was likely to lead the consumer to believe the purpose of the interview was to obtain credit information, rather than data about the health and activities of a claimant in an insurance claim." (ID 179)

Respondent contends that the ALJ's finding will not support an order because of its abandonment of the name "Retail Credit Company." (RAB 23 n.23) We agree that whatever the former name "Retail Credit" may have signified about the purpose of the investigation is certainly not implied by the name "Equifax Inc."

We nevertheless find that the form itself has the capacity to mislead. The form asks questions which to many consumers would seem more relevant to a credit check than to a claim investigation.[85] While responses to the questions might, in some cases, be relevant to the disposition of a claim, we find that the questionnaire, as written, has the capacity to deceive consumers into believing that they are the subject of a credit investigation.[86] Moreover, [66]there can be no doubt of the materiality of the deception, that, but for the deception, third-party claimants would be less likely to speak to the interviewer.

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[85] The form also seeks information which would seem relevant to an employment or other consumer or business report designed to elicit information about the individual's finances and his or her standing in the community.

[86] As to respondent's argument at RAB 24, we do not rely on witness Murray's testimony (Tr. 9596–97) but instead base our finding as to the misleading nature of the "Personal Interview" approach on our examination of the interview form. Nor, contrary to the ALJ (ID 178), do we make any finding that respondent intended consumers to be misled about the purpose of the "Personal Interview."

Respondent notes that the Privacy Protection Study Commission has criticized the use of the "pretext" interview, which it defined as one in which the interviewer "(1) pretends to be someone he is not; (2) pretends to represent someone he does not; or (3) misrepresents the true purpose of the interviewer. Mere silence on any or all of these points would not normally constitute a pretext interview." U.S. Privacy Protection Study Commission, *supra* p. 26, at 190. Respondent, however, can take little comfort from this language, as the "Personal Interview" approach has involved misrepresentations, as opposed to mere silence, about the purpose of the interview.

2. Acquisition of Medical Information

The complaint alleged that respondent has obtained medical information from physicians and other medical personnel on the basis of medical authorizations, signed by consumers, which misrepresent that the information would only be used by the insurance company to which the consumer executed the release when, in fact, a copy of the medical information is retained in respondent's files and is sometimes used in the preparation of subsequent reports for other customers. (Complaint, ¶¶ 11–13) The ALJ found a violation, based on his conclusion that the authorization forms

> would not put the consumer on notice that disclosure would be made to a third party consumer reporting agency which, for a portion of the relevant period, kept copies of such reports in its files and which could use such data in connection with unrelated transactions for which no authorization had been given. Consumers signing such authorizations did not give informed consent to the disclosure of such information to respondent.

ID 255. [67]

Respondent obtains medical information from physicians, hospitals, and clinics in connection with its Underwriting Medical History ("UMH") report and also certain claim reports. In the case of the UMH reports, the signed forms by which applicants for insurance authorize the release of their medical records are generally provided to Equifax by the insurance company. The language of the authorizations has varied. Some have authorized disclosure of information to respondent by name—the ALJ found that respondent has encouraged the use of such forms—while others have authorized the release of information to the "bearer," to the named insurance company, its "representative" or its "agent," or simply to the named insurance company. (ID 228; *see* RPF 219(a).)

In the case of claim investigations, respondent usually obtains authorization directly from the claimant and, in those cases, it uses its own form which expressly authorizes it to receive medical information about the claimant. (ID 229) Insurance companies, however, sometimes obtain authorizations from claimants and then furnish them to Equifax, and some authorize disclosure to a named insurance company or its "representative." (Tr. 10650)

Whether these authorizations are misleading, or whether consumers have not provided informed consent to the disclosure of medical information, depends on whether the information has actually been used in a manner consistent with the language of the authorization forms which they have signed. When the UMH service was first instituted, the company retained copies of UMH reports in its

regular alphabetical files and, although field representatives were instructed not to quote from a UMH report in a subsequent underwriting report, they could use the information as a "tip," that is, as a lead to assist them in the conduct of a new investigation. In July 1972, however, it became respondent's practice to retain copies of UMH reports for only 90 days[87] and in November 1973, respondent adopted the policy of destroying file copies as soon as the supervisor determines that the report has been properly prepared. (ID 237–39) As the judge found, in securing medical information for UMH reports, respondent now performs a "courier" service. (ID 227)

The filing procedures for medical information gathered in connection with a claim report have also changed. Before May 1974, claim reports were placed in the regular alphabetical files and medical information in these reports could be used as a "tip" in a subsequent investigation. Respondent also permitted disclosure in a new report that a prior claim report had been made together with the name of the doctor and hospital, and the dates and causes of [68]any hospital confinement. Beginning in May 1974, new claim reports were placed in separate files and previously prepared reports were to be pulled from the regular files and placed in the separate claim files. In December 1975, respondent instructed its staff not to retain medical information obtained in connection with a claim report. Instead, medical information was to be recorded on a separate form attached to the claim report and all copies of the medical attachment were to be destroyed once the report was mailed to the customer. (ID 240–44)

Because of the changes in respondent's procedures, and the limits imposed by the McCarran-Ferguson Act on our authority, we will not decide in this case whether an authorization can be valid only if the patient provides "informed consent" and, if so, what it takes for the consent to be informed. We do find, however, that so long as it was respondent's practice to retain for future use health information obtained pursuant to a signed authorization, those forms which authorized release to a named insurance company, without disclosure that the information would also be released to a reporting agency, had the tendency to mislead consumers into believing that the information would be released only to the insurance company. Forms which authorized release to a "representative" or the "bearer," again without disclosure that information would also be used by respondent, at least implied that disclosure would only be made to someone acting solely on behalf of the insurer. Consumers

[87] The copies were retained in case the original was lost, either in the mail or by the customer, and to assist in responding to questions about billing, and were not to be used in the preparation of other reports on the consumer. (ID 238)

would tend to infer from the language, and would be entitled to assume, that their authorizations would not be used by a reporting agency to obtain sensitive medical information which it would then be free to retain for future use.[88]

Moreover, the materiality of the misrepresentation is self-evident. It is obvious that consumers will be more likely to authorize release of medical records if they have been informed that the information will be used for a single purpose—the underwriting of a single insurance policy or adjustment of a particular claim—rather than for an undetermined number of future uses.[89] [69]

The forms were generally no longer misleading, however, once it became respondent's practice not to retain medical information for future use. Once respondent, in collecting medical information, acted only as a courier for the insurance companies, it was in fact no more than an agent, or representative, of the insurer.[90]

3. McCarran-Ferguson Act

a. "*Business of Insurance*"

The ALJ determined that the acts and practices he found unfair or deceptive are excluded from our authority by the McCarran-Ferguson Act because they are the "business of insurance."[91] We agree with the ALJ that the methods by which respondent collects [70]

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[88] It is immaterial that, in some cases, the misleading forms were prepared, and signatures were obtained, by insurance companies. Respondent, by its use of these forms to gather medical information and its subsequent retention of the information for uses which were not authorized by the consumer, participated in the deception. Indeed, it was respondent's retention and subsequent use of the information which made the insurance companies' authorization forms deceptive.

[89] On the propriety of basing findings of deception and materiality on the exercise of the Commission's expertise, *see* pp. 58–59 *supra*.

In challenging the ALJ's conclusion that consumers did not provide informed consent to the release of medical information to a consumer reporting agency, respondent contends that "[t]he release of medical information pursuant to an authorization is the act of a physician" and that "to find unfairness *by respondent*, the Administrative Law Judge has to draw the further inference * * * that respondent '*should* have been aware' of the 'fact' (not established by evidence in the record) that its customers obtained authorizations given without 'informed' consent." (RAB 41)

As noted earlier, our finding does not turn on any failure to provide "informed consent" but instead on the deceptive nature of the authorization forms. Complaint counsel were under no burden to show that the deception in these forms was never remedied by additional disclosures furnished by insurance companies or physicians.

[90] While forms which authorized disclosure to a named insurance company may have been misleading, we are not persuaded that any deception was material.

[91] The McCarran-Ferguson Act provides in relevant part:

> No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insurance: *Provided*, That after June 30, 1948, * * * the Sherman Act, * * * the Clayton Act, * * * and the Federal Trade Commission Act, as amended * * *, shall be applicable to the business of insurance to the extent that such business is not regulated by State Law.

15 U.S.C. 1012.

information for insurers are immunized from Section 5, but only to the extent the information is collected for use in connection with the underwriting or spreading of an insurance risk. When, as in the past, information has been collected for a variety of uses, clarity of analysis requires that we distinguish between collection of information for business of insurance uses and collection of information for non-insurance uses.

The McCarran-Ferguson Act renders the federal antitrust laws and the FTC Act inapplicable to the business of insurance insofar as such business is regulated by state law and is not subject to the "boycott" exception in Section 3(b) of the Act. In creating the exemption,

> Congress was concerned with the type of state regulation that centers around the contract of insurance * * *. The relationship between insurer and insured, the type of policy which could be issued, its reliability, interpretation, and enforcement—these were the core of the "business of insurance."

SEC v. *National Securities, Inc.*, 393 U.S. 453, 460 (1969). "[T]he underwriting or spreading of risk is a critical determinant in identifying insurance." *Group Life & Health Insurance Co.* v. *Royal Drug Co., Inc.*, 440 U.S. 205, 213 (1979).

Decisions whether to grant an application for an insurance policy are the essence of "the underwriting of * * * risk." No part of an insurance-related transaction could be more within the core of the business of insurance. The adjustment of claims is likewise at the core of the "business of insurance," as it bears directly on the interpretation and enforcement of the insurance policy.[92] [71]

Complaint counsel properly acknowledge that a firm need not be an insurer to be "in the business of insurance." (CAB 56)[93] *See also*

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[92] Although "[t]he primary elements of an insurance contract are the spreading and underwriting of a policyholder's risk," *Royal Drug Co., supra*, 440 U.S. at 211 (emphasis added), we are not persuaded by complaint counsel of the materiality of the fact that "to the extent that the indirect interview was used in connection with investigations of third party claimants * * *, the information furnished in the report would be used in connection with a claimant who was not a policyholder." (CRB 42) We cannot see how the determination of a claim submitted by a third party is any less the business of insurance than the resolution of a claim made by the policyholder. *See* R. Keeton, *Insurance Law* § 1.2(a) (1971) ("Insurance is an arrangement for transferring and distributing risk. It is an arrangement under which one (called an insurer) contracts to do something that is of value to another (*usually called an insured but sometimes called a beneficiary*) upon the occurrence of a specified harmful contingency.") (emphasis added) (section cited in *Royal Drug, supra*, 440 U.S. at 211). The insurer's payment to a third-party tort claimant involves the "spreading * * * of a policyholder's risk," and directly benefits the policyholder, since it satisfies a claim which might otherwise have been made against the policyholder.

Royal Drug, of course, affirms that not all insurer activities that ultimately affect the insurer's costs in settling claims, and the level of its premiums, are part of the business of insurance. In so doing, it raises but does not resolve the complex policy and factual issues involved in the process of defining the outer limits of the business of insurance. Since this case involves practices that clearly constitute the business of insurance, we need not reach those definitional questions here or attempt to identify a bright line dividing all aspects of the business of insurance from those activities which do not so qualify.

[93] Complaint counsel's acknowledgment is fully consistent with *Royal Drug's* holding that the Act exempts the "business of insurance" rather than the "business of insurance companies." 440 U.S. at 232–33.

Providence Washington Ins. Co., 89 F.T.C. 345, 401 (1977). It follows that an insurance company's election to contract with a non-insurer to gather information it deems important to its determination whether to underwrite a risk or to grant a claim—an activity which, if performed by its own employees, could only be viewed as the business of insurance—does not, by itself, alter the coverage of the McCarran-Ferguson Act exemption.

We also observed in *Providence Washington,* however, that "[w]here [McCarran-Ferguson Act] protection is sought for the activities of non-insurers, we think it especially critical that the transaction(s) in question be analyzed with precision, to ensure that the mere involvement of an insurance contract is not used to confer blanket immunity upon a wide range of activities [72]that are not the business of insurance." *Id.* at 401. *See also Peacock Buick, Inc.*, 87 F.T.C. 379, 381 (1976), *aff'd,* 553 F.2d 97 (4th Cir. 1977).

Accordingly, the collection of information for use in both McCarran-Ferguson insurance transactions and non-insurance transactions cannot be said to be only the "business of insurance;" moreover, the fact that the information is collected primarily for use in insurance transactions is insufficient to deprive the Commission of authority to reach the practice to the extent it is not the business of insurance. The collection of information for a multitude of insurance and non-insurance uses can more accurately be described as the business of collecting and using information—the business of a consumer reporting agency—than as the business of insurance. The ALJ, however, explaining his conclusion that respondent's retention of medical information, originally gathered for the use of insurers in the "underwriting or spreading of risk," is the business of insurance, stated:

> [I]t is apparent that securing such information initially is part of the business of insurance. In many instances, insurance companies perform such functions themselves. Respondent's practices in connection with the retention of medical information and the uses thereof which might otherwise violate the Federal Trade Commission Act arise directly out of the transactions subject to state regulation as the business of insurance. At best, it may be said that the activities here complained of are abuses by respondent in participating in the business of insurance.
> ID p. 220.[94] [73]

We disagree that merely because a practice "arise[s] directly out of

[94] Respondent also argues that "[s]ince inadequate disclosure is at the heart of the alleged violation, the proper remedial order, if any is justified, is one that affords more complete disclosure. And the McCarran Act undoubtedly places the authority for such regulation exclusively in the hands of state authorities." (R. Ans. 89) The Commission, however, may reach the practice if the failure to disclose is in connection with the gathering of information which is used for non-insurance purposes. Moreover, prohibitions against deception are not the only appropriate remedies for such violations. Another remedy is a ban on the continued use of information obtained as a result of the deception. *See* note 104 *infra.*

transactions subject to state regulation as the business of insurance" it is necessarily the business of insurance. *Royal Drug,* decided after the ALJ issued his initial decision, plainly rejects the notion that practices which may arise out of the business of insurance—the underwriting or spreading of risk—are necessarily immunized. Indeed, the contracts between the insurers and third-party providers of services at issue in *Royal Drug,* which the Court held outside the scope of the statutory exemption, could readily be characterized exactly as the ALJ described the practices in this case, as alleged "abuses by [the insurer] in participating in the business of insurance." (ID p. 220)[95] The practices themselves must be the business of insurance in that they directly relate to the contract between the insurer and the insured and involve the underwriting or spreading of risk. *Id.* at 212–15. The gathering of information to be used in an underwriting or claim report is the business of insurance; the gathering of information for use in a personnel, credit or other report not prepared in connection with the "underwriting or spreading of risk" is not. Any other result would contravene the rule that "[b]road exemptions from the antitrust laws and from major consumer protection legislation ought not be conferred lightly * * *." *Providence Washington, supra,* 89 F.T.C. at 407; *see Royal Drug, supra,* 440 U.S. at 231.

b. *State Regulation*

The business of insurance is immunized from federal law only insofar as it is regulated by the states. McCarran-Ferguson Act, Section 2(b). We agree with respondent that those practices in this case which are the business of insurance are also regulated by state law and that, accordingly, they are beyond the reach of Section 5.

As of August 1979, 45 states had adopted laws based on the Model Unfair Practices Act for Insurance ("Model Act"). *See* 2 National Ass'n of Ins. Commissioners, *Model Regulation Service,* 900.11 (August 1979).[96] The Model Act prohibits any "individual, corporation * * * and any other legal entity engaged in the business of insurance * * *," Model Act, Section 2(a), from "[m]aking, publishing, disseminating, circulating or placing before the public, * * * an advertisement, announcement or *statement* containing any assertion, representation or statement with respect to the business [74]of

[95] The Court did not reach the question whether the policies offered by the respondent health insurers were the business of insurance within the meaning of the Act. 440 U.S. at 230 n.37.

[96] The Model Act appears at 2 *Model Regulation Service, supra,* at 900.1 *et seq.* (January 1977).

insurance * * * which is untrue, deceptive or misleading." Model Act, Section 4(2) (emphasis added).[97] This prohibition amounts to "state regulation" within the meaning of Section 2(b) of the McCarran-Ferguson Act.[98]

The deceptive interviewing practices and medical authorization forms shown in this record appear to be clearly within the scope of the prohibition as they involve statements made by persons "engaged in the business of insurance" "with respect to the business of insurance,"[99] and complaint counsel have not contended that, insofar as they are the business of insurance, these practices are outside the scope of the Model Act. Nor have complaint counsel asserted that these statutory provisions are "mere pretense." *National Casualty Co., supra,* 357 U.S. at 564.[100] [75]

4. Violations and Order

In view of the McCarran-Ferguson Act, only the gathering of information by deceptive means for use in the preparation of non-insurance reports, or the actual use of the information for such non-insurance purposes, would violate Section 5. We will not bar

[97] Under the Model Act, violations of its prohibitions may subject the alleged violator to a cease and desist order. Model Act, Sections 7, 8. Section 7(a), as amended in 1977, also authorizes the state Commissioner of Insurance to proceed against unfair or deceptive acts or practices which are not specifically defined in Section 4.

[98] The Supreme Court, in *FTC* v. *National Casualty Co.*, 357 U.S. 560, 564 (1958), held that in view of state legislation adopted by nearly all of the states prohibiting unfair insurance advertising and authorizing enforcement through a scheme of administrative supervision, the practices at issue were subject to state regulation.

[99] In addition to those states which have enacted the Model Act, other states have adopted laws regulating unfair trade practices which contain provisions prohibiting untrue, deceptive or misleading statements similar to that contained in Section 4 of the Model Act. *See, e.g.,* Wash. Rev. Code Ann. Section 48.30.040 (1947); Wis. Stat. Ann. Section 628.34 (1976) (West).

[100] We are not persuaded by complaint counsel's presentation of the difficulties a state would face in attempting to protect its citizens against a report which was prepared and used in other states. (CAB 66) This is, accordingly, not a case in which the state laws in question cannot, or do not, adequately address the practices in question. *See FTC* v. *Travelers Health Ass'n,* 362 U.S. 293 (1960); *American General Ins. Co.,* 81 F.T.C. 1052 (1972); 89 F.T.C. 557 (1977), *remanded,* 589 F.2d 462 (9th Cir. 1979).

Respondent, citing *United Corp.* v. *FTC,* 110 F.2d 473 (4th Cir. 1940), contends that, because "it has already eliminated the spillover effects of claim investigations upon its non-insurance business," the Commission no longer has jurisdiction to reach its retention and use of information obtained by means of the indirect interview for non-insurance purposes. (R. Ans. 81)

In *United Corp.,* during the course of the administrative proceeding, the respondent had acquired the status of a packer, within the meaning of the Packers and Stockyards Act, 7 U.S.C. 181 *et seq.* (1976). The court noted that, once respondent became subject to the Packers and Stockyards Act, the Commission could no longer "grant effective relief," 110 F.2d at 476, because the respondent's status placed its operation outside the reach of the Commission's jurisdiction. In this matter, however, whether or not the McCarran-Ferguson Act exemption is jurisdictional, *compare Dexter* v. *Equitable Life Assurance Society,* 527 F.2d 233, 237 (2d Cir. 1975) *with National Casualty Co.* v. *FTC,* 245 F.2d 883, 888 (6th Cir. 1957), *aff'd,* 357 U.S. 560 (1958), respondent's practices that are not the business of insurance remain within the scope of Section 5, and an order prohibiting use of information for non-insurance purposes would, therefore, be "effective." The Commission may conclude, from a respondent's past violations (for example, unfair or deceptive acts or practices not part of the business of insurance) that there is a "cognizable danger" the violations will be repeated. *See* pp. 77-78 *infra.* Under respondent's reasoning, unfair or deceptive practices would be outside our authority unless we could determine that, as of the precise time an order issued, violations were still occurring. We believe it enough that the record support a conclusion that an order is needed to prevent, or to remedy, violations of Section 5, as limited by the McCarran-Ferguson Act.

respondent from using for non-insurance purposes information obtained through the indirect interview (in connection with the business of insurance), since these uses, particularly in credit reports but also in personnel and other non-insurance reports, would appear to be consistent with the representations implicit in the "Personal Interview" form.[101] The only uses [76]which would seem to be "unfair or deceptive" are immunized by the McCarran-Ferguson Act.[102]

We are persuaded by complaint counsel, however, that there is sufficient evidence to support an inference that medical information obtained through the use of misleading authorizations has been used in credit, personnel selection, and, perhaps, other reports which are not prepared as part of the business of insurance, in violation of Section 5.

Respondent has instructed its field representatives that "reference files are one of the Field Representative's most valuable tools" and that "[r]eference file information can help [the field representative] to make more accurate, thorough, and conclusive reports by: * * * [r]educing unnecessary duplication of effort[,] * * * [i]ndicating points deserving special attention[,] * * * [and] [a]iding in better source selection." (CX 666K) (Field Representative Manual)

Respondent's Credit Reporting Manual advised field representatives that "[f]ile information can be used to advantage on Credit Reports" and noted that "reports made for insurance or other purposes" could be used "as a source to secure leads." (CX 665N) The record also includes testimony that file information is normally consulted by employees engaged in the preparation of personnel reports. (Tr. 4430–31)

Moreover, as noted above, respondent's procedures allowed reference files containing medical information to be used as sources for leads in the preparation of other reports (presumably including non-insurance reports) until July 1972, in the case of the UMH reports and May 1974, in the case of claim reports, [77]and it should be inferred that such information actually was consulted in the preparation of non-insurance reports.[103]

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[101] Until 1971, respondent explicitly represented that the purpose of the interview was to update the individual's credit file. We cannot conclude from this record that this use is materially different from use in personnel reports or the other kinds of non-insurance reports at issue in this case.

[102] Complaint counsel have not persuaded us that we should upset the ALJ's implied finding that, at least since 1966, the indirect interview has always been used in connection with "business of insurance" reports. (ID 178, 181) Although the ALJ did find that "pretexts" were used in some work other than claims, he also found that in 1966 the pretext interview was supplanted by the Credit File Audit procedure. (ID 168 & n.58)

[103] Respondent appeals (RAB 41–44) from the judge's implied finding that the use in a subsequent investigation of medical information as a tip has had the effect of disclosing confidential information to sources to whom leading questions might be asked (ID 246, 249) and his finding that, in any case, use of medical information as a tip breaches confidentiality because "use of tip information necessarily influences an investigation irrespective of whether leading questions are asked." (ID 249 & n.79) It also appeals from his refusal to find that certain medical information is not privileged. (ID 249 n.78)

(Continued)

Finally, over complaint counsel's objection, the judge found that "[t]he extensive changes in respondent's procedures which ultimately eliminated the retention of medical reports, ha[ve] effectively prevented further unauthorized use of medical information." (ID 256) Although these changes appear to ensure that medical reports which respondent now obtains will not be retained for future use, the record does not show that respondent has destroyed those portions of its claim reports containing medical information which were filed before it put into effect the procedural changes cited by the ALJ. It had been respondent's practice to retain this information and the absence of evidence that the information has been destroyed supports an inference that some of this information remains in respondent's files.

In any case, we find that there is a "cognizable danger of recurrent violation" of Section 5, *SCM Corp.* v. *FTC, supra,* 612 F.2d at 708, in view of the persistency of the violations (ID 237–43), and the fact that respondent stopped retaining copies of new reports that included medical information only after the Commission commenced its investigation (and in the case of claim reports long after the Commission issued the complaint). "[W]ith corporations as with individuals, past conduct is probative of [78]future behavior," *Kraftco Corp., supra,* 92 F.T.C. at 419, and an inference may accordingly be drawn that, absent an order, the violations will be repeated in the future. *Id.* at 419–20. *See also Official Airline Guides, Inc.* v. *FTC,* No. 1217, slip op. at 5708 (2d Cir. Sept. 18, 1980), *petition for cert. filed,* No. 80–961 (U.S. Dec. 12, 1980) (where practice abandoned before the conclusion of the proceedings, "Commission has discretion to find that an order is warranted because of the possibility of unlawful recurrence of the activity").

We will order respondent to cease and desist from using medical information obtained by means of the misleading authorizations described in this opinion except in connection with reports the sole purpose of which is "the business of insurance."[104]

Respondent has not persuaded us that ID 246, ID 249, or ID 249 n.78 is erroneous. We note, however, that our judgment that respondent has violated Section 5 does not turn on any finding as to whether field representatives have disclosed confidential information to sources or on any finding that the medical information described in ID 249 n.78 is "privileged." As to ID 249 & n.79, we need not decide whether the use of medical information in respondent's files as a tip in a later investigation breaches the confidentiality of the information. We only observe that, in some cases, it was a non-insurance use of information obtained by means of a misleading authorization form.

[104] As to the propriety of prohibiting the use of information obtained by a respondent in violation of Section 5, *see Beneficial Corp.,* 86 F.T.C. 119, 179 (1975), *aff'd in part and rev'd in part on other grounds,* 542 F.2d 611 (3d Cir. 1976), *cert. denied,* 430 U.S. 983 (1977).

We recognize that Section 605 of the FCRA generally prohibits the reporting of adverse information which is more than seven years old and that Section 614 requires the updating of adverse information contained in an investigative consumer report. Respondent's practice was generally only to use adverse information in a previous

(Continued)

C. Misrepresentations of the Manner in Which Respondent Prepares its Reports

The complaint alleged that respondent has violated Section 5 by misrepresenting to customers how it prepares its consumer reports. Specifically, respondent was charged with having falsely represented to customers that (1) its reports are compiled through in-person interviews (rather than by telephone) and direct observations of consumers' physical surroundings, and (2) all sources listed in reports have actually been contacted by respondent's investigative personnel. The complaint also asserted that users of the reports would not rely on them as much in making a decision as to a consumer's eligibility for a benefit such as insurance, had the manner in which the reports were prepared been truthfully and factually represented. In fact, in certain instances, according to the complaint, users would not have rejected a consumer's application for a benefit such as insurance, or increased the rate for or canceled the consumer's insurance coverage, had the manner in which the information been gathered been truthfully and factually represented. (Complaint, ¶¶ 9, 10) [79]

The ALJ sustained the complaint allegation as to the use of in-person interviews and direct observations. He also found that respondent's employees have listed sources who had not actually been contacted, but did not find that the practice violated Section 5. Respondent appeals from the ALJ's findings regarding in-person interviews and direct observations, and complaint counsel appeal from the judge's failure to issue an order prohibiting the listing of sources who have not been interviewed.

The complaint did not assert that respondent has violated Section 5 by encouraging customers to purchase its reports on the basis of misrepresentations of their worth. Instead, it alleged that respondent's representations may induce customers to give more weight to information in the reports than they would if they understood how the reports had actually been prepared. The complaint also alleged that customers may be induced to take adverse action against the subject of a report (for example, by declining an insurance application) because of the misunderstanding induced by the misrepresentations. In view of Congress' concern about preventing the dissemination of reports containing inaccurate *adverse* information[105] and what we understand to be the thrust of the complaint, we will not sustain these complaint allegations unless we conclude that respon-

report as a "tip" and the FCRA would not prohibit such use, so long as the information was properly updated. As explained above, however, such use would violate Section 5.

[105] *See* pp. 6-7, 21 *supra*.

dent's representations have made it more likely that users of the information would take adverse actions against consumers than they otherwise would have taken had they not been misled.

Respondent concentrates its appeal on a challenge to the legal theory which supports this portion of the complaint. Respondent asserts that the judge's findings should be set aside because of the lack of any evidence that respondent's customers have been deceived into buying a service. (RAB 31–32) Respondent, however, offers no explanation why Section 5's prohibition against "unfair or deceptive acts or practices in or affecting commerce" should be confined to acts or practices which mislead the victim "into buying something which he might not otherwise have bought." (RAB 31–32) Although these are probably the most common "unfair or deceptive acts or practices," our cases have also addressed other deceptions "in or affecting commerce," practices ranging from failures to disclose that responses to advertisements will be followed by a visit by a salesperson (*Encyclopedia Britannica,* 87 F.T.C. 421, 530 (1976), *aff'd,* 605 F.2d 964 (7th Cir. 1979), *cert. denied,* 100 S.Ct. 1329 (1980); *Mather Hearing Aid Distributors, Inc.,* 78 F.T.C. 709, 740 (1971)), to misrepresentations that legal action will be taken if a debt is not promptly paid (*e.g., Trans World Accounts, Inc.,* 90 F.T.C. 350 (1977), *aff'd in part and rev'd and remanded in part,* 594 F.2d 212 (9th Cir. 1979)), and misrepresentations to prospective employees of the training [80] or income they will receive (*e.g., Encyclopedia Britannica, Inc., supra,* 87 F.T.C. at 527–28).

Cases holding that a claim is not material unless complaint counsel show that the consumer, if not deceived, would be less likely to buy the product, *e.g., Leonard F. Porter, Inc., supra,* simply articulate the standard to be used in the most common of the cases involving unfair or deceptive acts or practices, those addressing misrepresentations which might induce a consumer to purchase a product. They do not hold that the Commission may infer materiality only where a claim makes it more likely that a consumer will purchase a product.[106]

Nevertheless, although the complaint is sound in theory, the record compiled in this case does not support a finding of liability. We affirm the ALJ's findings that respondent has misrepresented the extent to which it relies on face-to-face interviews as opposed to interviews conducted over the telephone, and that it has impliedly represented that some items of information are based on direct

[106] Respondent also claims that "a finding of violation of Section 5 by the Commission based on a failure to disclose what it deems to be a material fact relating to persons other than those to whom the representations were made would be a wholly unwarranted extension of the Commission's powers." (RAB 32) Nevertheless, if there are misrepresentations, they are about the products, that is, the reports respondent sells to its customers.

observations when, in fact, they are not. (ID 198–201, 211, 214–15) The record, however, does not support an inference that the misrepresentations have made it more likely that users of the information will take adverse action against consumers.

At least two underwriters called by complaint counsel testified that they understood interviews with applicants and sources are sometimes conducted by telephone. (Tr. 1088, 2634) We are dubious that underwriters generally assume that, in the absence of an express representation in the report, any particular applicant or source has been the subject of a face-to-face interview, since the record shows that they realize some interviews are conducted by telephone.[107] We are unwilling to speculate whether [81]these customers would give any less weight to a particular piece of information if they had a more precise understanding of the extent to which respondent's employees use the telephone. Moreover, although the judge correctly found that descriptions of the applicant and of his or her home and neighborhood impliedly (and in some cases falsely) represent that they are based on direct observations made by the investigator (ID 201, 204–05, 210–11), we lack sufficient evidence to conclude that the manner in which information has been gathered is more likely to lead to the misreporting of adverse information.[108] [82]

[107] The ALJ found that some underwriters construed a statement in a report that the applicant had been interviewed as representing that there had been a face-to-face interview. (ID 204) However, it is difficult to see how this assumption would make it more likely that the underwriter would take adverse action against the subject of the report. Applicants would be unlikely to provide adverse information about themselves in telephone interviews which would not be revealed in face-to-face interviews and underwriters could not be expected to regard adverse information supplied by the applicant over the telephone as particularly unreliable. If anything, underwriters would likely be concerned that adverse information had been overlooked if the applicant had not been the subject of a face-to-face interview.

[108] The ALJ found that "[c]ertain of respondent's field representatives have reported information concerning the appearance of the subject of the report or his home or physical surroundings, when they did not personally observe the subject of the report or his physical surroundings * * *." (ID 211) Several of the witnesses cited in the finding testified that they used the telephone because, in view of their production quotas, they did not have time to observe personally the applicant or the applicant's home and neighborhood. Only two of the witnesses, however—Mr. Buckley and Ms. Wallace— testified that they reported *adverse* information about the applicant or his or her surroundings. (Tr. 1349, 3009)

Complaint counsel proposed the following finding as to Mr. Buckley's testimony: "Mr. Buckley testified that 'fudging' information about an applicant's home is too specific. However, 'you can decline a case sitting in the office if you know the area. * * *.'" (CPF 221) We agree with complaint counsel's characterization of Mr. Buckley's testimony. Because he apparently did not fabricate information about the applicant's home and his testimony does not indicate the kind of information he would report about the applicant's surroundings, we cannot find that this former employee's use of the telephone resulted in the reporting of inaccurate adverse information or misrepresentations as to how he had obtained adverse information.

Similarly, Ms. Wallace, while testifying as to how she reported information concerning the "environment" in which an applicant for life insurance lived, stated that "by working in the same area all the time, I knew pretty much what the area was like and what each specific area was like and so * * * I would mark it okay unless it was one of the really, really bad areas." (Tr. 3005) Immediately following this testimony, however, she testified that if she obtained over the telephone information on the applicant's "living conditions," she "always marked that favorable." (*Id.*) There is no evidence that the information Ms. Wallace reported about the applicant's environment was inaccurate or was not based on her personal observation, albeit not necessarily an observation occasioned by that particular application.

Finally, Judge von Brand found that some field representatives have listed on their reports sources whom they did not actually interview, either in-person or by telephone, and that some report users give more credence to report information which purports to be based on more than one source. (ID 216–17) He nevertheless made no finding that this practice violates Section 5 and did not order any relief addressed specifically to these findings.[109]

Although the ALJ found that "[g]enerally field representatives did not fake sources in those instances where unfavorable * * * information was developed" (ID 402), the record includes some evidence of the listing of "fake" sources of adverse information. (ID 394) In view of the materiality of the number of sources listed (ID 216–17), we find that there is adequate evidence that the falsification of sources makes it more likely that adverse actions will be taken against consumers by users of the information. We therefore conclude that the faking of sources of adverse information is unfair or deceptive.

Like the ALJ, we are not, however, persuaded of the need for an order provision addressed specifically to this practice. Respondent already prohibits its employees from listing sources they have not interviewed, and it has been respondent's policy to discharge employees who violate that rule.[110] Although respondent's production quotas have induced some employees to list fake sources,[111] we are convinced that the relief we have ordered with respect to the pressures to produce adverse information will at least remove any incentives to falsify sources of such information. We have [83]no reason to suspect that an order specifically prohibiting falsification of sources of adverse information would add anything useful to the remedy ordered to eliminate pressures to produce adverse information.

V. Scope of Order

Respondent challenges the scope of the order entered by the ALJ on the ground that it applies "to corporate entities whose products and services have no rational relationship to 'the facts and circumstances of the particular case.'" (RAB 8) More specifically, respondent urges, assuming *arguendo* that any order is justified by the record, that the order "be [framed] in terms of the activities, or types of activities, shown by the record to be conducted by Equifax

[109] *But see* ¶¶ I.B., II.G.-I. of the ALJ's order. (ID pp. 277, 281–82)

[110] *See* note 34 *supra.*

[111] *See* p. 20 *supra.*

Services." (RAB 9 n.8) We agree, but we believe that the ALJ's order is so limited.

We reject respondent's challenge as entirely without merit—the order is expressly limited to the types of activities conducted by Equifax Services, which were the subject of this proceeding.[112] The breadth of a Commission order is governed by whether "the remedy selected has [a] reasonable relation to the unlawful practices found to exist." *FTC* v. *Colgate-Palmolive Co., supra,* 380 U.S. at 394-95; *see also United Biscuit Co.* v. *FTC,* 350 F.2d 615, 623 (7th Cir. 1965), *cert. denied,* 383 U.S. 926 (1966). In addition, Commission orders need not be directed only to violations actually shown on the record but may generally prohibit similar acts and practices. *See, e.g., Moog Industries Inc.* v. *FTC,* 238 F. 2d 43, 52 (8th Cir. 1956), *aff'd* 355 U.S. 411 (1958). In our view, the order in this case is fully consistent with these principles.

The record shows that subsidiaries of Equifax Inc. other than Equifax Services, for example, Retailers Commercial Agency, engage in activities similar to and sometimes overlapping those of Equifax Services. (CX 665H, I)[113] Indeed, respondent's Chief Executive Officer testified:

> Equifax, Inc., is the parent corporation of some 14 companies and divisions, some [84] of which are separately incorporated and some are autonomous operating divisions of Equifax, Inc. These various companies perform for special markets. However, they are all in the information industry, fundamentally furnishing business information to businesses and others who need to have information on which to base a business decision.

Tr. 4847-48. In addition, respondent called as witnesses two employees, both of whom served simultaneously as field representatives for Equifax Services (or Retail Credit Company) and as managers of Retailers Commercial Agency offices. (Tr. 12280, 12585) Another witness called by respondent, a manager of sales administration for Equifax (Tr. 6870), testified that, while the activities involved in producing certain telephone reports relating to employment experience are "almost handled exclusively by Retailers Commercial Agency" (Tr. 6881), an Equifax Services field representative might "do this type of report" in cities "other than the major metropolitan areas," where there was no Retailers Commercial office. (Tr. 6882) Moreover, the Credit Reporting Manual, which respondent provided

[112] Complaint counsel agree with the ALJ's exclusion from the order of credit reports prepared by Credit Bureau, Inc., of Georgia, Credit Bureau of Montreal Ltd., and Credit Marketing Services.

[113] Respondent notes that it "recognize[s] the need, if an order is entered, to cover the activities which are the subject of this proceeding even if they are subsequently transferred to another division or subsidiary • • •" (RAB 9 n.8) and agrees with complaint counsel that, if an order issues, it need not be restricted to a single subsidiary. (RRB 4 n.3)

to its field representatives, describes the Retailers Commercial Agency as

> a credit reporting organization, serving not only credit customers of the Retail Credit Company [now Equifax Services] but also local retail merchants, financial institutions, mortgage loan agencies, and other businesses engaged in consumer credit transactions.

CX 665 H. It notes that "[f]iles and record information are maintained to provide prompt and protective information for the users of its service" (*id.*) and states:

> In those locations where there is both a Retail Credit Company Branch Office and a Retailers Office, the Retailers Commercial Agency completes all Credit Reports including those received by Retail Credit Company. On the other hand Retail Credit Company completes all Character Financial Reports for these locations. If the credit inquiries are located outside of the Retailers territory, they are handled by Retail Credit Company.
> CX 665 H, I. [85]

Because respondent has offered no explanation as to how the consumer-related information-gathering activities of other subsidiaries which are subject to the ALJ's order differ from those of Equifax Services, we reject its request that we somehow attempt to tailor the order to the precise kinds of reports prepared by Equifax Services.[114]

Final Order

This matter having been heard by the Commission upon the cross-appeals of respondent and complaint counsel from the initial decision and upon briefs and oral argument in support thereof and opposition thereto, and the Commission for the reasons stated in the accompanying opinion having determined to affirm in part and reverse in part the initial decision:

It is ordered, That the initial decision of the administrative law judge be adopted as the findings of fact and conclusions of law of the Commission, except to the extent inconsistent with the accompanying opinion.

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[114] We have, however, narrowed the coverage of the order to "consumer reports," "investigative consumer reports" and "file" as those terms are defined in Section 603 of the FCRA, and deleted the judge's reference to "other reports containing information about consumers." The latter reference might be broad enough to include reports which are outside the scope of this proceeding. *See* note 56 *supra.*

As part of its general attack on the scope of the order entered by the ALJ, respondent also argues that "[i]n several instances, the order * * * enjoins any and all violations of various sections of the FCRA, whereas the evidence introduced by complaint counsel with respect to such sections related *exclusively* to narrow, specific practices of respondent." (RAB 7) (emphasis in original) In this connection, respondent cites four order provisions, each of which the Commission has narrowed.

Other findings of fact and conclusions of law of the Commission are contained in the accompanying opinion.

It is further ordered, That the following order to cease and desist be, and it hereby is, entered:

I

It is ordered, That respondent Equifax Inc., a corporation, its successors and assigns, and its officers, agents, representatives, and employees, directly or through any corporation, subsidiary, division, or other device, in connection with the collection, preparation, assembly, sale, or distribution of consumer reports, investigative consumer reports, and files, as "consumer report," "investigative consumer report," and "file" are defined in Section 603(d), (e) and (g) of the Fair Credit Reporting Act (Pub. Law No. 91-508, 15 U.S.C. 1681 *et seq.)* ("the Act") and interpreted in the accompanying Opinion of the Commission (except credit reports prepared by Credit Bureau, Inc. of Georgia, Credit Bureau of Montreal, Ltd., and Credit Marketing Services), shall cease and desist from:

A. Representing, directly or by implication, during the preparation of any report, that investigative personnel employed by Equifax are agents or employees of the company to which the consumer who is the subject of the report has applied for a benefit.

B. Submitting consumer report information to any of its customers who has previously received a consumer report regarding the same consumer, unless: in response to the order of a court having jurisdiction to issue such an order; in accordance with the written instructions of the consumer to whom it relates; or respondent has reason to believe the requester intends to use the information for a permissible purpose as set out in Section 604 of the Act.

C. (1) Rewarding or punishing employees, or representing to employees that they will be rewarded or punished, on the basis of the amount of adverse information (*i.e.*, information which may have, or may reasonably be expected to have, an unfavorable bearing on a consumer's eligibility or qualification for credit, insurance, employment or other benefit, including information which may result, or which may reasonably be expected to result, in a denial of, or increased costs for such benefits) or the proportion, or number, of consumer reports or investigative consumer reports they prepare which contain adverse information about or relating to the consumers who are subjects of said reports; or (2) Encouraging employees, directly or indirectly, to produce a specified number, or proportion, of reports containing adverse information.

D. Using any system of quality audits or any other plan or procedure whereby the performance of branch offices, regions, or other organizational units, or individuals, with respect to the production of adverse information, is ranked against that of other organizational units or individuals, or against previous performance by the same organizational units or individuals.

E. Including in a consumer report concerning employment at an annual salary of less than $20,000 any notice or other statement that indicates directly or indirectly by means of boilerplate language the existence of items of adverse information, the disclosure of which is prohibited by Section 605 of the Act; *provided, however,* that language notifying the customer of the statutory limitations on the reporting of adverse information may be included in the type of consumer report to which this paragraph applies if it is included in all such reports, regardless of whether a particular consumer's file contains adverse information which the statute prohibits from being reported; and *provided further,* that it is accompanied by an explanation that the notification is included in all reports of the type to which this paragraph applies and is not intended to imply the existence of obsolete adverse information which may not be reported.

F. Misrepresenting to any consumer who requests information concerning himself or herself in respondent's files, the consumer's rights to obtain disclosure by telephone under Section 610 of the Act.

G. Failing:

1. To make available to any consumer who requests information concerning himself or herself in respondent's files, in person or by mail, at the consumer's option, all forms which he or she must execute in connection with the requirements of Section 610 of the Act to receive disclosure to which the consumer is entitled under the Act and this order; and

2. To inform the consumer: that he or she has the right to disclosure upon proper identification, by telephone if he or she pays any toll charge, or in person, at the consumer's option; and what constitutes proper identification.

H. Failing to give disclosure required by Section 609 of the Act to any consumer who has requested disclosure, has provided proper identification as required by respondent under Section 610 of the Act, and has paid or accepted any charges which may be imposed under Section 612 of the Act.

I. Failing, when giving consumers disclosure, to disclose the nature and substance of all information (excluding medical information as defined in Section 603(i) of the Act) in its files on the

consumer at the time of the request, as required by Section 609 of the Act.

J. Requiring a consumer, as a prerequisite to disclosing information from the consumer's file pursuant to Section 609 of the Act, to fill out or sign a form which authorizes respondent to conduct a reinvestigation of any item the consumer may dispute, or to transmit the results of such reinvestigation to persons to whom it has previously reported the disputed information or which authorizes any business, organization, professional person or anyone else to give full information and records about said consumer to respondent; or interposing any other similar condition or requirement which exceeds those specified in Section 610 of the Act.

K. Failing within a reasonable period of time to reinvestigate any item of information in a consumer's file, the completeness or accuracy of which is disputed by the consumer, unless it has reasonable grounds to believe the dispute is frivolous or irrelevant, as required by Section 611(a) of the Act.

L. Furnishing, directly or indirectly, other than for reports prepared solely for use in the business of insurance, medical information, as defined in Section 603(i) of the Act, obtained in response to a written authorization signed by a consumer, unless the authorization clearly identifies respondent as a recipient of the medical information.

II

It is further ordered, That respondent deliver a copy of this order to all present and future employees who are engaged in the preparation of consumer reports and investigative consumer reports or who are engaged in the disclosure or reinvestigation of information required by the Act.

It is further ordered, That respondent distribute a copy of this order to each of its operating divisions and subsidiaries.

III

It is further ordered, That respondent notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondent, such as dissolution, assignment, or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries, or any other change in the corporation which may affect compliance obligations arising out of the order.

IV

It is further ordered, That respondent shall, within sixty (60) days after service upon it of this order, file with the Commission a report, in writing, setting forth in detail the manner and form in which it has complied with this order.

Commissioner Pitofsky did not participate.

IN THE MATTER OF

MURATA MANUFACTURING CO., LTD.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF SECTION 5 OF THE FEDERAL TRADE COMMISION ACT AND SECTION 7 OF THE CLAYTON ACT

Docket C-3053. Complaint, Dec. 16, 1980—Decision, Dec. 16, 1980

This consent order requires, among other things, "Murata," a Japanese manufacturer and seller of electronic components, including various types of ceramic capacitors, to divest itself of the Arizona Division of Erie Technological Products, Ltd. (ETP), to a Commission-approved buyer within nine months from the effective date of the order. Should Murata fail to divest ETP's Arizona Division in the specified time, it must divest the entire company to an eligible party within the four months following the initial divestiture period. Respondent is further required to hold ETP's business and assets completely separate and apart from its business and assets pending divestiture, and barred from acquiring, without prior Commission approval, certain firms engaged in the manufacture or sale of ceramic capacitors.

Appearances

For the Commission: *Steven R. Newborn, Sandra G. Wilkof* and *Virginia L. Snider.*

For the respondent: *W. Clayton Sparrow, Jr., Hurt, Richardson, Garner, Todd & Cadenhead,* Atlanta, Ga., and *Calvin Collier, Hughes, Hubbard & Reed,* Washington, D.C.

COMPLAINT

The Federal Trade Commission, having reason to believe that the respondent, Murata Manufacturing Co., Ltd. ("Murata"), subject to the jurisdiction of the Commission, has entered into an agreement providing for the acquisition of a majority of the stock of Erie Technological Products, Ltd. ("ETP"), which, if consummated, would violate Section 7 of the Clayton Act, as amended (15 U.S.C. 18), and Section 5 of the Federal Trade Commission Act, as amended (15 U.S.C. 45); that said agreement constitutes a violation of Section 5 of the Federal Trade Commission Act, as amended; and that a proceeding in respect thereof would be in the public interest, hereby issues its Complaint, pursuant to Section 11 of the Clayton Act (15 U.S.C. 21) and Section 5(b) of the Federal Trade Commission Act (15 U.S.C. 45(b)), stating its charges as follows:

I.

DEFINITIONS

1. For the purposes of this Complaint, the following definitions apply:

(a) A "*capacitor*" is an electrical energy storage device constructed of electrodes (conducting layers) separated by dielectric (insulating) material and included within code 3675 of the 1972 Standard Industrial Classification Manual. Capacitors are used in almost all electrical and electronic equipment.

(b) A "*ceramic capacitor*" is a capacitor incorporating ceramic material as the dielectric material, included within codes 3675080 through 3675086 and 3675089 of the 1972 Standard Industrial Classification Manual.

(c) A "*single layer ceramic capacitor*" is a ceramic capacitor constructed of two electrodes separated by one layer of ceramic dielectric material. Single layer ceramic capacitors may be shaped as discs, plates or tubes, included within code 3675080 of the 1972 Standard Industrial Classification Manual.

(d) A "*monolithic (or multilayer) ceramic capacitor*" is a ceramic capacitor consisting of many layers of electrodes and ceramic dielectrics which are sintered at high temperatures to form a monolithic block, included within codes 3675081–3675086 of the 1972 Standard Industrial Classification Manual.

(e) A "*fixed capacitor*" is a capacitor of which the capacitance (energy storing capability) is fixed at a given level at manufacture.

(f) A "*variable capacitor*" is a capacitor designed and manufactured to provide various ranges of capacitance, rather than a single capacitance rating, and the capacitance of which can be adjusted manually after insertion into circuitry, included within code 3675089 of the 1972 Standard Industrial Classification Manual. A ceramic variable capacitor is a variable capacitor incorporating ceramic material as the dielectric material.

II.

MURATA MANUFACTURING CO., LTD.

2. Murata is a corporation organized and existing under the laws of Japan.

3. Murata manufactures and sells electronic and electrical components including, but not limited to, capacitors, piezoelectric products, resistors, tuners, active filters, and CR networks. Murata

has subsidiaries and manufacturing operations in the United States, Germany and the Far East, and its products are distributed in more than thirty countries worldwide. Murata had 1979 sales of over $200 million.

4. Murata does business in the United States through and with its wholly-owned subsidiary, Murata Corporation of America ("MCA"). MCA, with headquarters at Marietta, Georgia, sells products manufactured by Murata and manufactures and sells fixed ceramic and variable capacitors.

5. In 1979, Murata ranked among the top eight sellers of fixed ceramic capacitors in the United States (with a 4.4% market share) and second in sales of single layer ceramic capacitors (with a 10.4% market share). Murata was the sixth largest seller of ceramic variable capacitors (with a 5.7% market share) in the United States.

6. At all times relevant herein, Murata has been and is now engaged in commerce within the meaning of the Clayton Act, as amended, and is a corporation whose business is in or affecting commerce within the meaning of the Federal Trade Commission Act, as amended.

III.

ERIE TECHNOLOGICAL PRODUCTS, LTD.

7. ETP is a corporation organized and existing under the laws of Canada.

8. James J. Walsh, an American citizen and the company's president, owns and controls the largest block of ETP's stock. The remaining stock is owned by 23 other shareholders.

9. ETP manufactures and sells passive electronic components and assemblies including capacitors, noise interference filters, rectifiers and other products used in electronic and electrical applications. ETP has manufacturing and testing facilities in Erie, State College, and Carlisle, Pennsylvania; Tucson, Arizona; Nogales, Mexico; Canada; and Germany. In 1979, ETP's worldwide sales were over $40 million.

10. ETP ranks among the eight largest sellers in the United States of all fixed ceramic capacitors (with a 4.4% market share), and among the four largest sellers of single layer ceramic capacitors (with a 9.4% market share). It is the second largest seller of ceramic variable capacitors (with a 23.3% market share) in the United States.

11. At all times relevant herein, ETP has been and is now engaged in commerce within the meaning of the Clayton Act, as

amended, and is a corporation whose business is in or affecting commerce within the meaning of the Federal Trade Commission Act, as amended.

IV.

THE ACQUISITION

12. On November 30, 1979, Murata and ETP entered into a purchase agreement providing for the acquisition by Murata of 75% of ETP's stock for a purchase price of up to $5,200,000. Under the terms of the agreement, Murata has the option to acquire the remaining 25% of each shareholder's stock at an escalating rate.

V.

TRADE AND COMMERCE

13. The relevant geographic market is the entire United States.
14. The relevant product markets are:

(a) the manufacture and sale of all fixed ceramic capacitors;
(b) the manufacture and sale of single layer ceramic capacitors;
(c) the manufacture and sale of ceramic variable capacitors.

15. Concentration in the manufacture and sale of the relevant products is high.

VI.

EFFECTS OF THE ACQUISITION

16. The effects of the proposed acquisition may be to substantially lessen competition or tend to create a monopoly in the relevant markets enumerated in Paragraphs 13 and 14 of this Complaint in the following ways, among others:

(a) it will eliminate substantial actual competition between Murata and ETP in the relevant markets;
(b) it will significantly increase the already high levels of concentration in the relevant markets;
(c) it will further raise the barriers to entry that exist in the relevant markets;
(d) the competitive benefits of internal expansion and innovation may be eliminated; and
(e) customers of ceramic capacitors, single layer ceramic capaci-

tors, and ceramic variable capacitors and ultimate consumers of products incorporating such products may be denied the benefits of free and open competition.

VII.

VIOLATIONS CHARGED

17. The proposed acquisition set forth in Paragraph 12, if consummated, would violate Section 7 of the Clayton Act, as amended, 15 U.S.C. 18, and would violate Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45.

18. The purchase agreement described in Paragraph 12 violates Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45.

Decision And Order

The Federal Trade Commission, having initiated an investigation of the proposed acquisition of Erie Technological Products, Ltd. ("ETP") by Murata Manufacturing Co., Ltd. ("Murata"), and Murata having been furnished thereafter with a copy of a draft of complaint which the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge Murata with violations of the Federal Trade Commission Act and the Clayton Act; and

Murata, its attorneys, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by Murata of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by Murata that the law has been violated as alleged in such complaint, and waivers provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that Murata has violated the said Acts, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Murata is a corporation organized, existing and doing business under and by virtue of the laws of Japan with its principal executive offices at 26-10, 2-Chome, Tenjin, Nagaokakyo-shi, Kyoto 617, Japan.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of Murata, and the proceeding is in the public interest.

ORDER

I.

It is ordered, That for the purposes of this order the following definitions shall apply:

1. "*Murata*" means Murata Manufacturing Co., Ltd., a corporation organized, existing, and doing business under and by virtue of the laws of Japan with its principal offices at 26-10, 2-Chome, Tenjin, Nagaokakyo-shi, Kyoto 617, Japan, as well as its officers, employees, agents, its parents, divisions, subsidiaries, affiliates, successors, assigns, and the officers, employees or agents of Murata's parents, divisions, subsidiaries, affiliates, successors or assigns.

2. "*ETP*" means Erie Technological Products, Ltd., a corporation organized, existing, and doing business under and by virtue of the laws of Canada with its principal offices at Suite 408, 1 Eva Rd., Etobicoke, Ontario, Canada, as well as its officers, employees, agents, its parents, divisions, subsidiaries, affiliates, successors, assigns, and the officers, employees or agents of ETP's parents, divisions, subsidiaries, affiliates, successors or assigns. "ETP" also means the entire company, including all assets, properties, titles to property, interests, rights and privileges of whatever nature, tangible and intangible, including but not limited to all real property, buildings, inventory, customer lists, tradenames, patents, patent applications, trademarks and all other property of whatever description presently owned or operated by ETP with all additions, replacements and improvements hereafter made to ETP.

3. "*Divested Products*" means all ceramic disc capacitors, ceramic plate capacitors, ceramic variable capacitors, ceramic tubular capacitors, and ceramic high voltage capacitors manufactured by ETP on or within three years prior to the effective date of this order.

4. "*Arizona Division*" means all assets, properties, titles to property, interests, rights and privileges of whatever nature, tangible and intangible, including but not limited to all real property, buildings, machinery, equipment, raw materials, inventory, customer lists, tradenames, patents, patent applications, trademarks, orders

for purchase of Divested Products from ETP that are unfilled on the date of the divestiture, and all other property of whatever description presently owned or operated by ETP for the manufacture of the Divested Products located in the case of tangible property in State College, Pennsylvania, Tucson, Arizona, and Nogales, Mexico, with all additions, replacements, and improvements hereafter made to the Arizona Division and such additional property of ETP that Murata determines to include in the Arizona Division. The term "Arizona Division" excludes all: (1) real estate and buildings located in State College, Pennsylvania; (2) other property located in State College, Pennsylvania, that the Commission, Murata, and the Eligible Person (as defined below) may agree is not necessary for the manufacture of the Divested Products; (3) debts and liabilities (except trade accounts payable and not overdue, accrued salaries, payroll taxes, payroll taxes withheld, accrued interest, insurance, utilities, and other similar operating expenses, to the extent these liabilities do not exceed accounts receivable); and (4) future leasehold obligations relating to ETP's facilities in Tucson, Arizona, and Nogales, Mexico.

5. "*Eligible Person*" means any individual, corporation (including subsidiaries thereof), partnership, joint venture, trust, unincorporated association, other business or legal entity, or any combination thereof, approved by the Commission. Such approval shall be in the sole discretion of the Commission.

6. "*Initial Divestiture Period*" shall mean a period ending nine months from the date of issuance of this order, except that if prior to the expiration of such nine month period, Murata has proposed a person as an Eligible Person and the Commission has neither approved nor disapproved of such person, then such nine month period shall be extended until thirty days following the Commission's approval or disapproval of such person as an Eligible Person. In no event shall the initial divestiture period be extended more than once.

II.

It is further ordered, That within four months after the end of the Initial Divestiture Period, Murata shall divest absolutely ETP to an Eligible Person, unless within the Initial Divestiture Period Murata shall have divested absolutely the Arizona Division to an Eligible Person.

III.

It is further ordered, That divestiture under paragraph II shall be in a manner which preserves the assets and business divested as a going concern and as a viable competitor.

IV.

It is further ordered, That pending divestiture under paragraph II required by this order:

A. Murata shall operate ETP as a separately managed subsidiary, separately maintaining its own financial books and records, auditors, employees and management. All earnings and profits of ETP shall be retained by ETP and shall not be distributed to Murata or any third party as dividends or in any other form.

B. Murata: (1) shall exert no control over or influence on or interfere in any way in any of the business decisions or operations of ETP; (2) shall not cause ETP, directly or indirectly, to adopt policies preferred, suggested, or dictated by Murata; (3) shall not change ETP's existing policies or methods of operation. Furthermore, no Murata officer, director, employee, representative, or agent shall serve in any ETP position and no Murata officer, director, employee, representative or agent shall serve on ETP's Board of Directors.

C. Murata shall refrain from consolidating, directly or indirectly, its manufacturing, planning, purchasing, marketing, sales, research and development, personnel, or any other operations with those of ETP, *provided,* that Murata may continue to use ETP's office space and computer facilities in Germany, to the limited extent it is already using those facilities as of the date this agreement is accepted by the Commission for placement on the public record.

D. Murata shall refrain from taking any action, directly or indirectly, which would cause any changes or alterations to be made in ETP's business or operations or organization, including, but not limited to, changes in the executive, management, personnel, research and development, manufacturing, marketing, and distribution aspects of ETP.

E. Murata shall refrain from interfering with ETP's presently used trademarks and tradenames and ETP shall continue to be free to use such trademarks and tradenames to identify products, and Murata shall not use such trademarks and tradenames to identify any products other than those manufactured by ETP.

F. Murata shall refrain from taking any actions with respect to

ETP likely to diminish ETP's sales or interfere with its corporate opportunities.

G. Murata shall refrain from marketing and/or selling its products through the same representatives or employees through which ETP markets and/or sells its products, except to the extent to which Murata's products and ETP's products were marketed and/or sold through the same representatives prior to November 30, 1979.

H. Murata shall refrain from promoting the products of ETP as its own products.

I. Murata shall refrain from buying or using any advertising that promotes the products of Murata and ETP together or discloses the relationship between the two companies.

J. Murata shall refrain from engaging in joint selling of Murata products and products of ETP.

K. Murata shall refrain from, directly or indirectly, selling, disposing of, or causing to be transferred any assets, property, or business of ETP, except that ETP may sell or transfer manufactured products in the ordinary course of business.

L. Murata shall refrain from mortgaging or pledging the assets of ETP pursuant to any loan transaction in which the borrower is Murata, or any entity other than ETP, except in connection with divestiture pursuant to paragraph II.

M. Murata shall refrain from causing ETP to guarantee any debts or obligations pursuant to any loan transaction in which the borrower is Murata, or any entity other than ETP, except in connection with divestiture of the Arizona Division pursuant to paragraph II.

N. Murata shall refrain from making available or communicating to ETP any confidential or proprietary information, and Murata shall not seek to obtain or exploit, directly or indirectly, any of ETP's trade secrets, manufacturing processes, patents, know-how, formulas or other technical information, unpublished price lists, customer lists, non-public financial and accounting books and records, or any other competitively sensitive information.

O. Murata shall hold in strict confidence and shall not divulge to any third party or use for its own or any third party's benefit any confidential information which Murata has obtained or may obtain from ETP since November 30, 1979, except for the limited purpose of effecting divestiture pursuant to paragraph II.

P. Murata shall provide the Federal Trade Commission with written notice immediately upon termination, resignation, retirement, or transfer of any officer or director or senior executive of ETP.

Q. During the life of this agreement and for the purpose of assuring compliance herewith, duly authorized representatives of the Federal Trade Commission shall be permitted, upon written request and reasonable notice to Murata, to interview officers, directors, and employees of Murata and ETP and examine documents, at reasonable times and in the presence of Murata counsel (if Murata employees) and ETP counsel (if ETP employees), regarding matters covered by this agreement.

V.

It is further ordered, That the divestiture ordered and directed by this order shall be made in good faith and shall be absolute and unqualified; *provided, however,* that an Eligible Person may give, and Murata may accept and enforce, any bona fide lien, mortgage, deed of trust or other form of security on all or any portion of the assets or business divested. If a security interest is accepted, in no event may such security interest give Murata a right to participate in the operation or management of such assets or business. In the event that Murata, as a result of the enforcement of any bona fide lien, mortgage, deed of trust or other form of security interest, reacquires possession of the assets divested, then Murata shall redivest the reacquired assets, as a going concern and as a viable competitor, to an Eligible Person within six months of the reacquisition.

VI.

It is further ordered, That, for a period of ten years from the date of issuance of this order, Murata, its parents, divisions, subsidiaries, affiliates, successors, or assigns, shall not, directly or indirectly, acquire any stock, share capital, or equity interest in any concern, corporate or noncorporate, engaged in the manufacture or sale in or to the United States of ceramic capacitors, without the prior approval of the Federal Trade Commission, if such concern:

A. is incorporated in the United States or organized under the laws of one of the United States or has its principal offices within the United States; or

B. manufactures ceramic capacitors in the United States; or

C. had annual net sales of ceramic capacitors of five million dollars or more in or into the United States in the most recently completed calendar year prior to the date of the requested approval.

VII.

It is further ordered, That Murata shall, within sixty days from the date of issuance of this order and every sixty days thereafter until divestiture is completed, submit in writing to the Commission a report setting forth in detail the manner and form in which Murata intends to comply, is complying, and has complied with the terms of this order and such additional information relating thereto as may from time to time reasonably be required. All such reports shall include a summary of contacts or negotiations with anyone for the specified assets, the identity of all such persons, and copies of all written communications to and from such persons. After divestiture is completed, Murata shall submit in writing annual reports showing the manner and form of compliance with this order.

VIII.

It is further ordered, That for a period of ten years from the date of issuance of this order, Murata shall notify the Commission at least thirty days prior to any change in Murata which may affect compliance with the obligations arising out of this consent order, such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries, or any other change in the corporation.

TABLE OF COMMODITIES*

DECISIONS AND ORDERS

	Page
Analgesics, non-prescription internal	1
Art materials	625, 638, 809
Athlete's foot products	194
Bearings	752
Bodybuilding products	783
Ceramic capacitors	1116
Consumer credit	120
Consumer credit reports	844
Copper ore	600
Correspondence courses	208
Cosmetics and related products	51
Debt collection services	196, 823, 825
Denture cushions	757
Discount merchandise	603
Electronics	172, 178, 184, 189
Gasoline additives	380
General merchandise	60
Grocery products	42
Hair replacement	73
Industrial machines	352
Motor vehicles	18, 32, 111, 134, 362
Non-motorized vehicles	619
Pesticide products	826
Portland cement and gypsum wallboard	795
Rainwear	335, 340
Recreational equipment	151
Reference materials	778
Repossessed motor vehicles	37
Retail credit	32
Retail sale of drugs	197
Silver products	83
Sun care products	612
Titanium dioxide pigment	*653*
Trade shows	126
Wearing apparel	145
Wine	*385*
Wool products	40

*Commodities involved in dismissing or vacating orders are indicated by *italicized* page reference.

INDEX*

DECISIONS AND ORDERS

Page

Acquiring Corporate Stock or Assets:
- Acquiring corporate stock or assets—
  - Federal Trade Commission Act 42, 151, 197, 352, 612, 795, 1116
- Joint ventures 151

Advertising Falsely or Misleadingly:
- Knowingly by advertising agent 1
- Business status, advantages or connections—
  - Business methods and policies 208
  - Contracts and obligations 208
  - Reputation, success, or standing 208
- Comparative data or merits—
  - Competitors' products 1
- Content 1
- Demand, business or other opportunities 208
- Earnings and profits 208
- Endorsements, approval and testimonials 208, 783
- Government approval, action, connection or standards 826
- History of product or offering 73, 783
- Opportunities 208
- Promotional sales plans 208, 783, 826
- Qualities or properties of product or service 73, 826
  - Analgesic 1
  - Durability or permanence 757
  - Medicinal, therapeutic, healthful, etc. 1, 783
- Quality of product or service 208
- Results 1, 73, 208, 783
- Safety—
  - Product 73, 757, 826
- Scientific or other relevant facts 1, 73, 208, 757, 783
- Scientific tests 1
- Success, use or standing 208
- Unique nature or advantages 1
- Value 208

Claiming or Using Endorsements or Testimonials Falsely or Misleadingly:
- Claiming or using endorsements or testimonials falsely or misleadingly 208, 783

Coercing and Intimidating:
- Customers or prospective customers 51, 83, 145

Collecting, Assembling, Furnishing or Utilizing Consumer Reports:
- Confidentiality, accuracy, relevancy, and proper utilization—
  - Fair Credit Reporting Act 844
- Formal regulatory and/or statutory requirements—
  - Fair Credit Reporting Act 844

*Covering practices and matters involved in Commission orders. References to matters involved in vacating or dismissing orders are indicated by *italics*.

Page

Combining or Conspiring:
Combining or conspiring 625, 638
To control marketing practices and conditions 51, 83, 145, 625, 638, 809
To eliminate competition in conspirators' goods 809
To enforce or bring about resale price maintenance 51, 83, 145
To enhance, maintain or unify prices 51, 145, 809
To exchange future price information 625, 638, 809
To fix prices 625, 638, 809
To restrain or monopolize trade 51, 83, 145
To submit collusive bids 625, 638, 809
To terminate or threaten to terminate contracts, dealings, franchises, etc. 51, 83, 145
Corrective Actions and/or Requirements:
Corrective actions and/or requirements—
Corrective advertising 73
Disclosures 1, 18, 37, 51, 60, 73, 83, 111, 120, 134, 145, 208, 362, 625, 638, 757, 809, 826, 844
Displays, in-house 18, 362
Employment of independent agencies 60
Formal regulatory and/or statutory requirements 18, 844
Furnishing information to media 73, 362, 826
Maintain records 18, 60, 111, 120, 134, 208, 362, 625, 638, 783, 795, 809
Making supply of product(s) available to competitors 795
Recall of merchandise, advertising material, etc. 362
Refunds, rebates and/or credits 18, 37, 60, 111, 134, 208, 362
Restitution 625, 638, 809
Warranties 18
Cutting Off Supplies or Service:
Cutting off supplies or service 51, 83, 145
Threatening disciplinary action or otherwise 51, 83, 145
Delaying or Withholding Corrections, Adjustments or Action Owed:
Delaying or withholding corrections, adjustments or action owed 37, 51, 60, 134, 335, 340
Dismissal Orders *385, 653*
Disseminating Advertisements, etc. 1, 73, 619
Failing To Comply with Affirmative Statutory Requirements:
Fair Credit Reporting Act 844
Magnuson-Moss Warranty Act 18
Interlocking Directorates Unlawfully 172, 178, 184, 189
Interlocutory Orders 91, 162, 168, 205, 332, 346, 605, 650
Maintaining Resale Prices:
Contracts and agreements 83
Discrimination—
Against price cutters 51, 145
In favor of price maintainers 51, 145
Penalties 51, 83, 145
Refusal to sell 83
Systems of espionage—
Requiring information of price cutting 51, 83, 145
Misrepresenting Oneself and Goods:
Business status, advantages or connections—

Page

Business methods, policies, and practices 120
Financing activities 120
Personnel or staff 844
Goods—
Comparative data or merits 1
Content 1
Demand for or business opportunities 208
Earnings and profits 208
Formal regulatory and statutory requirements 18, 844
Guarantees 18
History of product 73, 783
Jobs and employment 208
Law or legal requirements 111, 120
Qualities or properties 1, 73, 757
Quality 208
Refunds 208
Results 1, 73, 208, 783
Scientific or other relevant facts 1, 73, 111, 208, 757, 783, 826, 844
Terms and conditions—
Sales contract 208
Tests, purported 1
Unique nature or advantages 1
Prices—
Additional costs unmentioned 111
Modifying Orders 32, 40, 126, 194, 196, 380, 600, 603, 752, 778, 823, 825
Neglecting, Unfairly or Deceptively, To Make Material Disclosure:
Content 1
Formal regulatory and/or statutory requirements—
Fair Credit Reporting Act 844
Magnuson-Moss Warranty Act 18
History of products 73, 783
Instruments' sale to finance companies 208
Limitations of product 208, 757
Prices—additional prices unmentioned 111
Qualities or properties 1, 73, 826
Safety 73, 619, 757, 826
Sales contract, right-to-cancel provision 208
Scientific or other relevant facts 1, 60, 73, 111, 208, 362, 757, 783, 826, 844
Terms and conditions 362
Sales contract 208
Offering Unfair, Improper and Deceptive Inducements To Purchase or Deal:
Earnings and profits 208
Opportunities in product or service 208
Scientific or other relevant facts 1, 208
Using Deceptive Techniques In Advertising 783

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